No. 15945

United States
Court of Appeals
for the Ninth Circuit

ALBERT GERSTEN, MYRON P. BECK and ANN H. BECK, MILTON GERSTEN and MARY GERSTEN, Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

Transcript of Record

Petitions to Review Decisions of The Tax Court of the United States

Phillips & Van Orden Co., Fourth and Berry Sts., San Francisco, Calif.—5-2-58

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INDEX

[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

NAMES AND ADDRESSES OF ATTORNEYS

JACOB SHEARER,
TANNENBAUM, STEINBERG & SHEARER,
Suite 300, 151 El Camino Drive,
Beverly Hills, California,

Attorneys for Petitioners.

CHARLES K. RICE,
Assistant United States Attorney General,

LEE A. JACKSON,
Attorney,
Department of Justice,
Tax Division,
Washington 25, D. C.,

Attorneys for Respondent.

APPEARANCES

For Petitioner:

JACOB SHEARER,
LEHMAN C. AARONS.

For Respondent:

GEORGE E. CONSTABLE.

The Tax Court of the United States

Docket No. 51226

ALBERT GERSTEN, Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

DOCKET ENTRIES

1953

Nov. 12—Petition received and filed. Taxpayer notified. Fee paid.

Nov. 13—Copy of petition served on General Counsel.

Nov. 12—Request for Circuit hearing in Los Angeles, Calif. filed by taxpayer. 11/27/53—Granted.

1954

Jan. 5—Answer filed by General Counsel.

Jan. 13—Copy of answer served on taxpayer—Los Angeles, Calif.

1955

Feb. 8—Hearing set April 25, 1955, Los Angeles, Calif.

Apr. 29—Hearing had before Judge Turner on the merits on petitioner's oral motion to consolidate dockets 51226 to 51242, incl.—Granted. Stipulation of facts filed at hearing. Briefs due 120 days from 4/29/55; Replies due 165 days from 4/29/55.

May 17—Transcript of Hearing 4/29/55 filed.

Aug. 24—Supplemental stipulation of facts, filed.

Aug. 26—Motion for extension to Sept. 6, 1955 to file brief filed by General Counsel. 8/29/55—Granted.

Aug. 29—Brief filed by taxpayer. (P) 9/28/55 copy served.

Sep. 6—Motion for extension of time to 9/27/55 to file brief, filed by General Counsel. 9/7/55—Granted.

Sep. 27—Brief filed by General Counsel.

Nov. 10—Motion for extension to 11/25/55 to file reply brief filed by taxpayer. 11/10/55—Granted.

Nov. 25—Reply Brief filed by petitioner. Copy served 11/28/55. Printed brief received 12/5/55.

Dec. 27—Motion for substitution of printed reply brief in place and stead of typewritten briefs heretofore filed, filed by petitioner. 2/3/56—Granted.

1956

Feb. 3—Order that the respondent is allowed 45 days from this date within which to file his reply brief, entered.

Mar. 16—Motion for extension to April 9, 1956 to file Reply Brief, filed by Respondent. Granted 3/19/56. Served 3/21/56.

Apr. 9—Reply Brief filed by Respondent. Served 4/10/56.

1957

Jun. 28—Findings of Fact and Opinion filed. Judge Turner. Decision will be entered under Rule 50. Served 6/28/57.

Oct. 25—Agreed computation.

Oct. 30—Decision entered. Judge Turner. Served 10/31/57.

1958

Jan. 24—Petition for Review by U. S. Court of Appeals, 9th Circuit with proof of service attached, filed by petitioner.

Feb. 5—Designation of Contents of Record on Review with proof of service, filed.

Feb. 14—Designation of additional portions of record on review with proof of service thereon, filed by Respondent.

Feb. 20—Order extending time for filing record on review and docketing petition for review, to April 24, 1958.

The Tax Court of the United States

Docket No. 51228

MYRON P. BECK and ANN H. BECK,
Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DOCKET ENTRIES

[Note: Docket Entries in Docket No. 51228 are the same as Docket No. 51226 except for the following]:

1954

Jan. 6—Answer filed by General Counsel.

Jan. 14—Copy of answer served on taxpayer, Los Angeles, Calif.

1958

Feb. 6—Designation of Contents of Record on Review with proof of service, filed.

The Tax Court of the United States

Docket No. 51229

MILTON GERSTEN and MARY GERSTEN,
Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DOCKET ENTRIES

[Note: Docket Entries in Docket No. 51229

are the same as Docket No. 51226 except for the following]:

1954

Jan. 6—Answer filed by General Counsel.

Jan. 14—Copy of answer served on taxpayer, Los Angeles, Calif.

1958

Feb. 6—Designation of contents of record on review with proof of service thereon, filed.

[Title of Tax Court and Docket No. 51226.]

PETITION

The above named petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his Notice of Deficiency dated August 24, 1953, and as a basis of his proceeding alleges as follows:

1. Petitioner is an individual whose residence is 6363 Wilshire Boulevard, Los Angeles 48, California. The return for the period here involved was a joint return of petitioner and of Bernice Ann Gersten, as husband and wife, and was filed with the Collector of Internal Revenue for the Sixth District of California.

2. The Notice of Deficiency (a copy of which is attached and marked Exhibit "A") was mailed to petitioner on August 24, 1953.

3. The deficiency as determined by the Commissioner is in income taxes as follows:

Year	Deficiency
1950 Income Tax	$10,429.15

The entire deficiency is in dispute.

4. The determination of tax set forth in the said notice of deficiency is based upon the following errors:

(a) Respondent erred in determining that long term capital gains received by petitioner in said year in respect of the liquidation of Lawrence Land Co. were understated in petitioner's Federal income tax return for said year by $6,120.78, and in failing to determine that petitioner overstated his long term capital gains in respect of said liquidation by $4,990.64.

(b) Respondent erred in determining that long term capital gains received by petitioner in said year in respect of the liquidation of Whittier Development Co. were understated in petitioner's Federal income tax return for said year by $5,893.80, and in failing to determine that petitioner overstated his long term capital gains in respect of said liquidation by $3,464.72.

(c) Respondent erred in determining that long term capital gains received by petitioner in said year in respect of the liquidation of Rex Land Co. were understated in petitioner's Federal income tax return for said year by $3,566.34.

(d) Respondent erred in determining that long term capital gains received by petitioner in said year in respect of the liquidation of J. Richard Co. were understated in petitioner's Federal income tax return for said year by $8,854.74.

(e) Respondent erred in determining that the return filed by petitioner and his wife, Bernice Ann

Gersten, for the taxable year 1950, constituted only a separate return of petitioner and not the joint return of petitioner and his said wife.

5. The facts upon which petitioner relies as a basis for this proceeding, are as follows:

(a) On or about March 15, 1950, petitioner purchased 60 shares of the stock of Lawrence Land Co. (hereinafter referred to as "Lawrence") for the sum of $6,000.00. Said 60 shares represented 40% of all of the stock of Lawrence issued and outstanding at all times material hereto.

(b) Lawrence was a corporation incorporated pursuant to the laws of the State of California on or about March 25, 1949, and on that date commenced to do business within the State of California.

(c) Lawrence's business consisted of the subdivision of unimproved land into residential lots, including the installation of subdivision improvements, the erection of residences or homes upon such lots, and the sale thereof.

(d) On December 31, 1950, Lawrence was finally wound up and dissolved, and on or about said date its assets were distributed to its stockholders proportionately to their stock holdings.

(e) Pursuant to the winding up and complete liquidation of Lawrence petitioner received as his proportion of the assets of Lawrence the sum of $78,382.40 in cash, and an undivided 40% interest in certain real property in the County of Los Angeles, State of California, which undivided interest had a then fair market value of $29,840.00. There

was also assigned to petitioner, in connection with said liquidation, a 40% interest in a certain contract, dated January 25, 1950, as amended February 9, 1950, between Lawrence and San Gabriel Valley Water Company (hereinafter referred to as "San Gabriel").

(f) In connection with the dissolution of Lawrence, petitioner and the other stockholders of Lawrence entered into a written agreement on December 26, 1950, in which said stockholders assumed and became responsible for all of the debts, obligations and liabilities of Lawrence. Said agreement was entered into in order to comply with sections 5000 and 5001 of the Corporations Code of the State of California pertaining to voluntary dissolutions of corporations.

(g) The undisputed amount of Lawrence's liability under the Excess Profits Tax Act of 1950, as amended, as of the time of its dissolution, was $12,476.68, and petitioner's obligation in respect thereof, pursuant to his assumption of liability under the agreement referred to in paragraph 5 (f) above, amounted to $4,990.64. Petitioner's accountant, at the time he prepared petitioner's 1950 Federal income tax return, failed to take into account said sum of $4,990.64 so assumed by petitioner and accordingly, overstated petitioner's long term capital gain in respect of the dissolution of Lawrence by the sum of $4,990.64.

(h) At all times material hereto San Gabriel was engaged in the business of supplying water to residences and other properties located in the dis-

trict in which the tract of real property of Lawrence was situated.

(i) Pursuant to said contract, San Gabriel agreed to extend its pipelines for the servicing of water to Lawrence's property upon payment to it by Lawrence of the sum of $31,021.00.

(j) Said contract further provided for contingent refunds to Lawrence by San Gabriel of all, or a portion, of the said sum of $31,021.00, up to the whole thereof.

(k) By the terms of said contract, the aggregate amount of such refunds, if any, was dependent upon the amount of gross revenue, if any, which San Gabriel might receive, within a limited period of time, from the sale of water to consumers within the tract being developed by Lawrence.

(l) At all times material hereto, neither Lawrence nor San Gabriel had any control over any purchases of water which such consumers might make from San Gabriel.

(m) On or about March 21, 1950, petitioner purchased 400 shares of the stock of Whittier Development Co. (hereinafter referred to as "Whittier") for the sum of $4,000.00, and thereafter and until the dissolution of Whittier owned 400 shares thereof. Said 400 shares represented 40% of all of the stock of Whittier issued and outstanding at all times material hereto.

(n) Whittier was a corporation incorporated pursuant to the laws of the State of California on or about August 20, 1948, and during the month of

July of 1949 commenced to do business within the State of California.

(o) Whittier's business consisted of the subdivision of unimproved land into residential lots, including the installation of subdivision improvements, the erection of residences or homes upon such lots, and the sale thereof.

(p) On December 28, 1950, Whittier was finally wound up and dissolved, and on or about said date, its assets were distributed to its stockholders proportionately to their stock holdings.

(q) Pursuant to the winding up and complete liquidation of Whittier petitioner received as his proportion of the assets of Whittier the sum of $77,160.27 in cash. There was also assigned to petitioner, in connection with said liquidation, a 40% interest in a certain contract, dated November 29, 1949, between Whittier and San Gabriel, and a 40% interest in a certain contract, dated March 10, 1950, between Whittier and San Gabriel.

(r) In connection with the dissolution of Whittier, petitioner and the other stockholders of Whittier entered into a written agreement on December 16, 1950, in which said stockholders assumed and became responsible for all of the debts, obligations and liabilities of Whittier. Said agreement was entered into in order to comply with sections 5000 and 5001 of the Corporations Code of the State of California pertaining to voluntary dissolutions of corporations.

(s) The undisputed amount of Whittier's liability under the Excess Profits Tax Act of 1950, as

amended, as of the time of its dissolution, was $8,661.79, and petitioner's obligation in respect thereof, pursuant to his assumption of liability under the agreement referred to in paragraph 5 (r) above, amounted to $3,464.72. Petitioner's accountant, at the time he prepared Petitioner's 1950 Federal income tax return, failed to take into account said sum of $3,464.72 so assumed by petitioner and accordingly, overstated petitioner's long term capital gain in respect of the dissolution of Whittier by the sum of $3,464.72.

(t) At all times material hereto San Gabriel was engaged in the business of supplying water to residences and other properties located in the district in which the tracts of real property of Whittier were situated.

(u) Pursuant to the contract dated November 29, 1949, San Gabriel agreed to extend its pipelines for the servicing of water to one of the tracts being developed by Whittier upon the payment to it by Whittier of the sum of $23,841.00.

(v) In said contract it further provided for contingent refunds to Whittier by San Gabriel of all, or a portion, of the said sum of $23,841.00.

(w) Pursuant to the contract dated March 10, 1950, San Gabriel agreed to extend its pipelines for the servicing of water to another of the tracts being developed by Whittier upon payment to it by Whittier of the sum of $5,214.00.

(x) Said contract further provided for contingent refunds to Whittier by San Gabriel of all, or a portion, of the said sum of $5,214.00.

(y) By the terms of said contracts, the aggregate amounts of such refunds, if any, were dependent upon the amount of gross revenue, if any, which San Gabriel might receive, within a limited period of time, from the sale of water to consumers within the tracts being developed by Whittier.

(z) At all times material hereto, Whittier had no control over any purchases of water which such consumers might make from San Gabriel.

(aa) On or about February 8, 1949, petitioner purchased 50 shares of the stock of Rex Land Co. (hereinafter referred to as "Rex") for the sum of $5,000.00. Said 50 shares represented 50% of all of the stock of Rex issued and outstanding at all times material hereto.

(bb) Rex was a corporation incorporated pursuant to the laws of the State of California on or about February 4, 1949, and on that date commenced to do business within the State of California.

(cc) Rex's business consisted of the subdivision of unimproved land into residential lots, including the installation of subdivision improvements, the erection of residences or homes upon such lots, and the sale thereof.

(dd) On November 8, 1950, Rex was finally wound up and dissolved, and on or about said date its assets were distributed to its stockholders proportionately to their stock holdings.

(ee) Pursuant to the winding up and complete liquidation of Rex petitioner received as his proportion of the assets of Rex the sum of $1,158.84 in

cash, and an undivided 50% interest in certain real property in the County of Los Angeles, State of California, which undivided interest had a then fair market value of $118,000.00. There was also assigned to petitioner, in connection with said liquidation, a 50% interest in a certain contract, dated February 3, 1949, between Albert Gersten and San Gabriel. Albert Gersten had executed said contract in his own name but for the benefit of Rex and subsequently, in February of 1949, assigned said contract to Rex.

(ff) At all times material hereto San Gabriel was engaged in the business of supplying water to residences and other properties located in the district in which the tract of real property of Rex was situated.

(gg) Pursuant to said contract, San Gabriel agreed to extend its pipelines for the servicing of water to Rex's property upon payment to it by Rex of the sum of $14,707.20.

(hh) Said contract further provided for contingent refunds to Rex by San Gabriel of all, or a portion, of the said sum of $14,707.20.

(ii) By the terms of said contract, the aggregate amount of said refunds, if any, was dependent upon the amounts of gross revenue, if any, which San Gabriel might receive, within a limited period of time, from the sale of water to consumers within the tract being developed by Rex.

(jj) At all times material hereto, Rex had no control over any purchases of water which such consumers might make from San Gabriel.

(kk) On or about July 10, 1947, petitioner purchased 1005 shares of the common stock of J. Richard Co. (hereinafter referred to as "Richard") for the sum of $10,050.00. Said 1005 shares represented 50% of all of the common stock of Richard issued and outstanding at all times material hereto.

(ll) Richard was a corporation incorporated pursuant to the laws of the State of California on or about July 10, 1947, and on that date commenced to do business within the State of California.

(mm) Richard's business consisted of the subdivision of unimproved land into residential lots, including the installation of subdivision improvements, the erection of residences or homes upon such lots, and the sale thereof.

(nn) On June 22, 1950, Richard was finally wound up and dissolved, and on or about said date its assets were distributed to its stockholders proportionately to their stock holdings.

(oo) Pursuant to the winding up and complete liquidation of Richard petitioner received as his proportion of the assets of Richard the sum of $38,202.12 in cash. There was also assigned to petitioner, in connection with said liquidation, a 50% interest in a certain contract, dated November 21, 1947, between Albert Gersten and San Gabriel, and a 50% interest in a certain contract, dated November 30, 1948, between Albert Gersten and San Gabriel. Albert Gersten had executed said contracts in his own name, but for the benefit of Richard, and subsequently, in November 1947 and December

1948 respectively, Gersten assigned said contracts to Richard.

(pp) At all times material hereto San Gabriel was engaged in the business of supplying water to residences and other properties located in the district in which the tracts of real property of Richard were situated.

(qq) Pursuant to the contract dated November 21, 1947, San Gabriel agreed to extend its pipelines for the servicing of water to one of the tracts being developed by Richard upon the payment to it by Richard of the sum of $23,764.00.

(rr) Said contract further provided for contingent refunds to Richard by San Gabriel of all, or a portion, of the said sum of $23,764.00.

(ss) Pursuant to the contract dated November 30, 1948, San Gabriel agreed to extend its pipelines for the servicing of water to one of the tracts being developed by Richard upon the payment to it by Richard of the sum of $15,258.00.

(tt) Said contract further provided for contingent refunds to Richard by San Gabriel of all, or a portion, of the said sum of $15,258.00.

(uu) By the terms of said contracts, the aggregate amounts of such refunds, if any, were dependent upon the amount of gross revenue, if any, which San Gabriel might receive, within a limited period of time, from the sale of water to consumers within the tracts being developed by Richard.

(vv) At all times material hereto, Richard had no control over any purchases of water which such consumers might make from San Gabriel.

(ww) Prior to December 1950, petitioner was married to one Lucille Gersten. On or about March 31, 1950, an interlocutory decree of divorce was granted to said Lucille Gersten and petitioner by the Superior Court of the State of California, in and for the County of Los Angeles. In November 1950 there was granted to petitioner, by a competent Court of Mexico having jurisdiction therein, a final decree of divorce from said Lucille Gersten, finally and completely dissolving the marriage which theretofore existed between petitioner and said Lucille Gersten.

(xx) On November 2, 1950, following said final decree of divorce, petitioner married his present wife, Bernice Ann Gersten, in Mexico.

(yy) On or about May 7, 1951, petitioner and said Bernice Ann Gersten executed and caused to be filed on or about said date their joint United States Individual Income Tax Return, with the Collector of Internal Revenue for the Sixth District of California. The time for the filing of said return had theretofore been extended by respondent, upon the request of petitioner and said Bernice Ann Gersten, to May 15, 1951.

(zz) Petitioner alleges that if the foregoing allegations set forth in paragraph 5, subparagraphs (g) and (s) above, with respect to the overstatement of long term capital gains for the taxable year 1950, together with the remaining allegations with respect to said taxable year, are determined to be correct, petitioner will be entitled to a refund with respect to said year 1950 based upon an overassessment in the amount of at least $2,113.84.

Wherefore, petitioner prays that this Court may hear the proceedings and determine that no deficiency is due from him for the taxable year 1950, but that petitioner is entitled to a refund for the said taxable year based upon an overassessment in the amount of at least $2,113.84; and that this Court grant such other general or special relief as may be by law provided.

/s/ JACOB SHEARER,
/s/ LEHMAN C. AARONS,
Counsel for Petitioner.

Duly Verified.

EXHIBIT "A"

Regional
1250 Subway Terminal Building
417 South Hill Street
Los Angeles 13, California

ARC-Ap:SF LA:90D:PAK

Aug. 24, 1953

Mr. Albert Gersten
6363 Wilshire Boulevard
Los Angeles 48, California

Dear Mr. Gersten:

You are advised that the determination of your income tax liability for the taxable year ended December 31, 1950 discloses a deficiency of $10,429.15, as shown in the statement attached.

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiency mentioned.

Within 90 days from the date of the mailing of

this letter you may file a petition with The Tax Court of the United States, at its principal address, Washington 4, D. C., for a redetermination of the deficiency. In counting the 90 days you may not exclude any day unless the 90th day is a Saturday, Sunday, or legal holiday in the District of Columbia, in which event that day is not counted as the 90th day. Otherwise Saturdays, Sundays, and legal holidays are to be counted in computing the 90-day period.

Should you not desire to file a petition, you are requested to execute, in duplicate, the enclosed form and forward it to the Assistant Regional Commissioner, Appellate, 1250 Subway Terminal Building, 417 South Hill Street, Los Angeles 13, California. The signing and filing of this form will expedite the closing of your return by permitting an early assessment of the deficiency, and will prevent the accumulation of interest, since the interest period terminates 30 days after receipt of the form, or on the date of assessment, or on the date of payment, whichever is earlier.

Very truly yours,

T. COLEMAN ANDREWS,
Commissioner of Internal Revenue,
/s/ By W. T. TIGNOR,
Associate Chief, Appellate Division.

PAKar:lae
Enclosures:
Statement
Form 1276
Agreement Form

Statement

ARC-Ap:SF LA:90D:PAK

Mr. Albert Gersten, 6363 Wilshire Boulevard, Los Angeles 48, California

Tax Liability for the Taxable Year Ended December 31, 1950.

Year: 1950. Income tax—Deficiency: $10,429.15.

In making this determination of your income tax liability careful consideration has been given to the report of examination dated September 23, 1952, to your protest dated November 6, 1952, and to the statements made at a hearing held on January 27, 1953.

You filed a joint return for the year 1950 with your wife Bernice Ann Gersten. It has been determined that, since under the laws of the State of California, an interlocutory decree of divorce from Lucille Gersten was in effect as of December 31, 1950, only a separate return will be recognized in accordance with Section 51(b)(1) of the Internal Revenue Code.

Accordingly, the amount of your income tax liability for this taxable year is determined herein on the basis of a separate return and the exemption claimed, in the joint return filed, with respect to said Bernice Ann Gersten is disallowed as a credit to you.

A copy of this letter and statement has been mailed to your representative, Mr. Jacob Shearer, 6535 Wilshire Boulevard, Los Angeles 48, Califor-

nia, in accordance with the authorization contained in the power of attorney executed by you.

Adjustments to Net Income
Taxable Year Ended December 31, 1950

Net income as disclosed by return	$190,104.35
Additional income and unallowable deductions:	
(a) Long-term capital gains	11,104.87
(b) Taxes disallowed	195.00
(c) Travel and entertainment expense disallowed	1,800.00
Total	$203,204.22
Reduction:	
(d) Income from partnerships	57.92
Net income adjusted	$203,146.30

Explanation of Adjustments

(a) It is determined that the correct amount of net long-term capital gain realized during this taxable year is $169,451.68 instead of the amount, $158,346.81, reported in your return or an increase of $11,104.87. The amount of such increase is determined upon the adjustments of the fair market values of your share of property received upon the liquidation of the corporations named below:

(1) J. Richard Co. fair market value increased	$ 8,854.74
(2) Whittier Development Co. fair market value increased	5,893.80
(3) Rex Land Co. fair market value increased	3,566.34
(4) Lawrence Land Co. fair market value increased	6,120.78
Total increase	$24,435.66
Long-term capital gain—50% of $24,435.66	$12,217.83
Less:	
(5) Capital loss carry-over	1,112.96
Net increase of long-term capital gain	$11,104.87

Explanation

(1) It is determined that the fair market value of water contracts received by you is $8,854.74. No value was reported by you upon such contracts.

(2) The fair market value of property received from Whittier Development Co. (to which no value was reported in your return) is determined in the following amounts:

Value of water contracts	$5,515.80
Value of refundable deposit	378.00
Increase as above	$5,893.80

(3) The fair market value of property received from Rex Land Co. (to which no value was reported in your return) is determined in the following amounts:

Fair market value of water contracts	$3,439.54
Fair market value of state tax claim	126.80
Net increase as above	$3,566.34

(4) The fair market value of water contracts (to which no value was reported in your return) received from Lawrence Land Co. is determined in the amount of $6,120.78.

(5) A capital loss carry-over, not previously claimed by you, is allowed in the amount of $1,112.96 and representing a capital loss carry-over from the taxable year ended December 31, 1949.

(b) It is determined that the correct deduction for social security taxes is the amount of $30.00 instead of the amount, $225.00, claimed in your return, or a decrease of $195.00.

(c) Items of travel and entertainment expense amounting to $1,800.00 have not been substantiated as proper deductions under section 23 (a) of the Internal Revenue Code and are disallowed.

(d) It is determined that the correct amount of your distributive share of the loss of the partnership, Superior Building Company, is $193.90 instead of the loss. $135.98, reported in your return, or an increase of $57.92.

Computation of Alternative Tax
Taxable Year Ended December 31, 1950

Net income adjusted	$203,146.30
Less: Excess of net long-term capital gain over net short-term capital loss	169,451.68
Ordinary net income	$ 33,694.62
Less: Exemptions	1,200.00
Balance, subject to surtax and normal tax	$ 32,494.62

Tentative surtax	$13,806.66	
Tentative normal tax at 3%	974.84	
Total tentative tax	$14,781.50	
Less: reduction under Sec. 12 (c) I.R.C.	1,346.34	
Partial tax		$ 13,435.16
Plus: 50 per cent of $169,451.68		84,725.84
Alternative tax		$ 98,161.00

Computation of Tax
Taxable Year Ended December 31, 1950

Net income adjusted		$203,146.30
Less: Exemptions		1,200.00
Balance, subject to surtax and normal tax		$201,946.30
Tentative surtax	$152,532.74	
Tentative normal tax at 3%	6,058.39	
Total tentative tax	$158,591.13	
Less: reduction under Sec. 12 (c), I.R.C.	13,293.15	
Total normal tax and surtax		$145,297.98
Alternative tax		$ 98,161.00
Correct income tax liability		$ 98,161.00
Income tax liability shown on return, account No. 5-315090		87,731.85
Deficiency of income tax		$ 10,429.15

Served: Nov. 13, 1953.

[Endorsed]: T.C.U.S. Filed Nov. 12, 1953.

[Title of Tax Court and Docket No. 51226.]

ANSWER

The Commissioner of Internal Revenue, by his attorney, Daniel A. Taylor, Chief Counsel, Internal Revenue Service, for answer to the petition of the above-named taxpayer, admits and denies as follows:

1, 2 and 3. Admits the allegations contained in paragraphs 1, 2 and 3 of the petition.

4. Denies the allegations of error contained in paragraph 4 of the petition and all subparagraphs thereunder.

5. (a) to (d), inclusive. Admits the allegations contained in subparagraphs (a) to (d), inclusive, of paragraph 5 of the petition.

(e), (f) and (g). Denies the allegations contained in subparagraphs (e), (f) and (g) of paragraph 5 of the petition.

(h), (i) and (j). Admits the allegations contained in subparagraphs (h), (i) and (j) of paragraph 5 of the petition.

(k) and (l). Denies the allegations contained in subparagraphs (k) and (l) of paragraph 5 of the petition.

(m) to (p), inclusive. Admits the allegations contained in subparagraphs (m) to (p), inclusive, of paragraph 5 of the petition.

(q), (r) and (s). Denies the allegations contained in subparagraphs (q), (r) and (s) of paragraph 5 of the petition.

(t) to (x), inclusive. Admits the allegations contained in subparagraphs (t) to (x), inclusive, of paragraph 5 of the petition.

(y) and (z). Denies the allegations contained in subparagraphs (y) and (z) of paragraph 5 of the petition.

(aa) to (dd), inclusive. Admits the allegations contained in subparagraphs (aa) to (dd), inclusive, of paragraph 5 of the petition.

(ee) Denies the allegations contained in subparagraph (ee) of paragraph 5 of the petition.

(ff), (gg) and (hh). Admits the allegations contained in subparagraphs (ff), (gg) and (hh) of paragraph 5 of the petition.

(ii) and (jj). Denies the allegations contained in subparagraphs (ii) and (jj) of paragraph 5 of the petition.

(kk) to (nn), inclusive. Admits the allegations contained in subparagraphs (kk) to (nn), inclusive, of paragraph 5 of the petition.

(oo). Denies the allegations contained in subparagraph (oo) of paragraph 5 of the petition.

(pp) to (tt), inclusive. Admits the allegations contained in subparagraphs (pp) to (tt), inclusive, of paragraph 5 of the petition.

(uu) to (zz), inclusive. Denies the allegations contained in subparagraphs (uu) to (zz), inclusive, of paragraph 5 of the petition.

6. Denies generally and specifically each and every allegation contained in the petition not hereinbefore expressly admitted, qualified or denied.

Wherefore, it is prayed that the determination of the Commissioner be approved.

/s/ DANIEL A. TAYLOR, REM,
Chief Counsel, Internal
Revenue Service.

Of Counsel: Woolvin Patten, Acting Regional Counsel, E. C. Crouter, Associate Appellate Counsel, R. E. Maiden, Jr., Assistant Appellate Counsel, Clayton J. Burrell, Special Attorney, Internal Revenue Service.

[Endorsed]: T.C.U.S. Filed Jan. 5, 1954.

[Title of Tax Court and Docket No. 51228.]

PETITION

The above named petitioners hereby petition for a redetermination of the deficiencies set forth by the Commissioner of Internal Revenue in his Notice of Deficiency dated August 24, 1953, and as a basis of their proceedings allege as follows:

1. Petitioners are individuals whose residence is c/o Mr. Ben Bisgeier, 9119 Sunset Boulevard, Los Angeles 46, California. The return for all of the periods here involved was a joint return of petitioners, as husband and wife, and were filed with the Collector of Internal Revenue for the Sixth District of California.

2. The Notice of Deficiency (a copy of which is attached and marked Exhibit "A") was mailed to petitioners on August 24, 1953.

3. The deficiencies as determined by the Commissioner are in income taxes as follows:

Year		Deficiency
1949	Income Tax	$1,340.00
1950	Income Tax	7,835.92
		$9,175.92

Of said amounts, the sum of $7,835.92, representing the deficiency for the year 1950, is in dispute.

4. The determination of tax set forth in the said notice of deficiency is based upon the following errors:

(a) Respondent erred with respect to the taxable year 1950 in determining that long term capital gains received by petitioners in said year in respect of the liquidation of Lawrence Land Co. were understated in petitioners' Federal income tax return for said year by $7,650.98, and in failing to determine that petitioners overstated their long term capital gains in respect of said liquidation by $6,238.34.

(b) Respondent erred with respect to the taxable year 1950 in determining that long term capital gains received by petitioners in said year in respect of the liquidation of Whittier Development Co. were understated in petitioners' Federal income tax return for said year by $5,893.80, and in failing to determine that petitioners overstated their long term capital gains in respect of said liquidation by $3,464.72.

(c) Respondent erred with respect to the taxable year 1950 in determining that long term capital gains received by petitioners in said year in respect of the liquidation of Rex Land Co. were understated in petitioners' Federal income tax return for said year by $3,566.34.

(d) Respondent erred with respect to the taxable year 1950 in determining that long term capital gains received by petitioners in said year in respect of the liquidation of J. Richard Co. were understated in petitioners' Federal income tax return for said year by $8,854.74.

5. The facts upon which petitioners rely as a basis for this proceeding, are as follows:

(a) All of the transactions here involved were those of petitioner, Myron P. Beck, and for convenience the term "petitioner" as hereinafter used in this paragraph will refer to petitioner, Myron P. Beck.

(b) On or about May 26, 1949, petitioner purchased 50 shares for the sum of $5,000.00, and on or about June 30, 1949, purchased 25 shares for the sum of $2500.00 of the stock of Lawrence Land Co. (hereinafter referred to as "Lawrence"). Said 75 shares represented 50% of all of the stock of Lawrence issued and outstanding at all times material hereto.

(c) Lawrence was a corporation incorporated pursuant to the laws of the State of California on or about March 25, 1949, and on that date commenced to do business within the State of California.

(d) Lawrence's business consisted of the subdivision of unimproved land into residential lots, including the installation of subdivision improvements, the erection of residences or homes upon such lots, and the sale thereof.

(e) On December 31, 1950, Lawrence was finally wound up and dissolved, and on or about said date its assets were distributed to its stockholders proportionately to their stock holdings.

(f) Pursuant to the winding up and complete liquidation of Lawrence petitioner received as his proportion of the assets of Lawrence the sum of $97,978.00 in cash, and an undivided 50% interest in certain real property in the County of Los Angeles, State of California, which undivided interest had a then fair market value of $37,300.00. There was also assigned to petitioner, in connection with said liquidation, a 50% interest in a certain contract, dated January 25, 1950, as amended February 9, 1950, between Lawrence and San Gabriel Valley Water Company (hereinafter referred to as "San Gabriel").

(g) In connection with the dissolution of Lawrence, petitioner and the other stockholders of Lawrence entered into a written agreement on December 26, 1950, in which said stockholders assumed and became responsible for all of the debts, obligations and liabilities of Lawrence. Said agreement was entered into in order to comply with sections 5000 and 5001 of the Corporations Code of the State of California pertaining to voluntary dissolutions of corporations.

(h) The undisputed amount of Lawrence's liability under the Excess Profits Tax Act of 1950, as of the time of its dissolution, was $12,476.68, and petitioner's obligation in respect thereof, pursuant to his assumption of liability under the agreement referred to in paragraph 5 (g) above, amounted to $6,238.34. Petitioner's accountant, at the time he prepared petitioner's 1950 Federal income tax return, failed to take into account said sum of $6,238.34 so assumed by petitioner and accordingly, overstated petitioner's long term capital gain in respect of the dissolution of Lawrence by the sum of $6,238.34.

(i) At all times material hereto San Gabriel was engaged in the business of supplying water to residences and other properties located in the district in which the tract of real property of Lawrence was situated.

(j) Pursuant to said contract, San Gabriel agreed to extend its pipelines for the servicing of water to Lawrence's property upon payment to it by Lawrence of the sum of $31,021.00.

(k) Said contract further provided for contingent refunds to Lawrence by San Gabriel of all, or a portion, of the said sum of $31,021.00 up to the whole thereof.

(l) By the terms of said contract, the aggregate amount of such refunds, if any, was dependent upon the amount of gross revenue, if any, which San Gabriel might receive, within a limited period of time, from the sale of water to consumers within the tract being developed by Lawrence.

(m) At all times material hereto, neither Lawrence nor San Gabriel had any control over any purchases of water which such consumers might make from San Gabriel.

(n) On or about July 11, 1949, petitioner purchased 500 shares of the stock of Whittier Development Co. (hereinafter referred to as "Whittier") for the sum of $5,000.00. On or about April 22, 1950, petitioner sold 100 of said shares for $1,000.00, and thereafter and until the dissolution of Whittier owned 400 shares thereof. Said 400 shares represented 40% of all of the stock of Whittier issued and outstanding at all times material hereto.

(o) Whittier was a corporation incorporated pursuant to the laws of the State of California on or about August 20, 1948, and during the month of July of 1949 commenced to do business within the State of California.

(p) Whittier's business consisted of the subdivision of unimproved land into residential lots, including the installation of subdivision improvements, the erection of residences or homes upon such lots, and the sale thereof.

(q) On December 28, 1950, Whittier was finally wound up and dissolved, and on or about said date, its assets were distributed to its stockholders proportionately to their stock holdings.

(r) Pursuant to the winding up and complete liquidation of Whittier petitioner received as his proportion of the assets of Whittier the sum of $77,160.27 in cash. There was also assigned to petitioner, in connection with said liquidation, a 40%

interest in a certain contract, dated November 29, 1949, between Whittier and San Gabriel, and a 40% interest in a certain contract, dated March 10, 1950, between Whittier and San Gabriel.

(s) In connection with the dissolution of Whittier, petitioner and the other stockholders of Whittier entered into a written agreement on December 16, 1950, in which said stockholders assumed and became responsible for all of the debts, obligations and liabilities of Whittier. Said agreement was entered into in order to comply with sections 5000 and 5001 of the Corporations Code of the State of California pertaining to voluntary dissolutions of corporations.

(t) The undisputed amount of Whittier's liability under the Excess Profits Tax Act of 1950, as of the time of its dissolution, was $8,661.79, and petitioner's obligation in respect thereof, pursuant to his assumption of liability under the agreement referred to in paragraph 5(s) above, amounted to $3,464.72. Petitioner's accountant, at the time he prepared petitioner's 1950 Federal income tax return, failed to take into account said sum of $3,464.72 so assumed by petitioner and accordingly, overstated petitioner's long term capital gain in respect of the dissolution of Whittier by the sum of $3,464.72.

(u) At all times material hereto San Gabriel was engaged in the business of supplying water to residences and other properties located in the district in which the tracts of real property of Whittier were situated.

(v) Pursuant to the contract dated November 29, 1949, San Gabriel agreed to extend its pipelines for the servicing of water to one of the tracts being developed by Whittier upon the payment to it by Whittier of the sum of $23,841.00.

(w) In said contract it further provided for contingent refunds to Whittier by San Gabriel of all, or a portion, of the said sum of $23,841.00.

(x) Pursuant to the contract dated March 10, 1950, San Gabriel agreed to extend its pipelines for the servicing of water to another of the tracts being developed by Whittier upon payment to it by Whittier of the sum of $5,214.00.

(y) Said contract further provided for contingent refunds to Whittier by San Gabriel of all, or a portion, of the said sum of $5,214.00.

(z) By the terms of said contracts, the aggregate amounts of such refunds, if any, were dependent upon the amount of gross revenue, if any, which San Gabriel might receive, within a limited period of time, from the sale of water to consumers within the tracts being developed by Whittier.

(aa) At all times material hereto, Whittier had no control over any purchases of water which such consumers might make from San Gabriel.

(bb) On or about February 8, 1949, petitioner purchased 50 shares of the stock of Rex Land Co. (hereinafter referred to as "Rex") for the sum of $5,000.00. Said 50 shares represented 50% of all of the stock of Rex issued and outstanding at all times material hereto.

(cc) Rex was a corporation incorporated pursu-

ant to the laws of the State of California on or about February 4, 1949, and on that date commenced to do business within the State of California.

(dd) Rex's business consisted of the subdivision of unimproved land into residential lots, including the installation of subdivision improvements, the erection of residences or homes upon such lots, and the sale thereof.

(ee) On November 8, 1950, Rex was finally wound up and dissolved, and on or about said date its assets were distributed to its stockholders proportionately to their stock holdings.

(ff) Pursuant to the winding up and complete liquidation of Rex petitioner received as his proportion of the assets of Rex the sum of $1,158.84 in cash, and an undivided 50% interest in certain real property in the County of Los Angeles, State of California, which undivided interest had a then fair market value of $118,000.00. There was also assigned to petitioner, in connection with said liquidation, a 50% interest in a certain contract, dated February 3, 1949, between Albert Gersten and San Gabriel. Albert Gersten had executed said contract in his own name but for the benefit of Rex and subsequently, in February of 1949, assigned said contract to Rex.

(gg) At all times material hereto San Gabriel was engaged in the business of supplying water to residences and other properties located in the district in which the tract of real property of Rex was situated.

(hh) Pursuant to said contract, San Gabriel agreed to extend its pipelines for the servicing of water to Rex's property upon payment to it by Rex of the sum of $14,707.20.

(ii) Said contract further provided for contingent refunds to Rex by San Gabriel of all, or a portion, of the said sum of $14,707.20.

(jj) By the terms of said contract, the aggregate amount of said refunds, if any, was dependent upon the amounts of gross revenue, if any, which San Gabriel might receive, within a limited period of time, from the sale of water to consumers within the tract being developed by Rex.

(kk) At all times material hereto, Rex had no control over any purchases of water which such consumers might make from San Gabriel.

(ll) On or about July 10, 1947, petitioner purchased 1005 shares of the common stock of J. Richard Co. (hereinafter referred to as "Richard") for the sum of $10,050.00. Said 1005 shares represented 50% of all of the common stock of Richard issued and outstanding at all times material hereto.

(mm) Richard was a corporation incorporated pursuant to the laws of the State of California on or about July 10, 1947, and on that date commenced to do business within the State of California.

(nn) Richard's business consisted of the subdivision of unimproved land into residential lots, including the installation of subdivision improvements, the erection of residences or homes upon such lots, and the sale thereof.

(oo) On June 22, 1950, Richard was finally

wound up and dissolved, and on or about said date its assets were distributed to its stockholders proportionately to their stock holdings.

(pp) Pursuant to the winding up and complete liquidation of Richard petitioner received as his proportion of the assets of Richard the sum of $38,202.12 in cash. There was also assigned to petitioner, in connection with said liquidation, a 50% interest in a certain contract, dated November 21, 1947, between Albert Gersten and San Gabriel, and a 50% interest in a certain contract, dated November 30, 1948, between Albert Gersten and San Gabriel. Albert Gersten had executed said contracts in his own name, but for the benefit of Richard, and subsequently, in November 1947 and December 1948 respectively, Gersten assigned said contracts to Richard.

(qq) At all times material hereto San Gabriel was engaged in the business of supplying water to residences and other properties located in the district in which the tracts of real property of Richard were situated.

(rr) Pursuant to the contract dated November 21, 1947, San Gabriel agreed to extend its pipelines for the servicing of water to one of the tracts being developed by Richard upon the payment to it by Richard of the sum of $23,764.00.

(ss) Said contract further provided for contingent refunds to Richard by San Gabriel of all, or a portion, of the said sum of $23,764.00.

(tt) Pursuant to the contract dated November

30, 1948, San Gabriel agreed to extend its pipelines for the servicing of water to one of the tracts being developed by Richard upon the payment to it by Richard of the sum of $15,258.00.

(uu) Said contract further provided for contingent refunds to Richard by San Gabriel of all, or a portion, of the said sum of $15,258.00.

(vv) By the terms of said contracts, the aggregate amounts of such refunds, if any, were dependent upon the amount of gross revenue, if any, which San Gabriel might receive, within a limited period of time, from the sale of water to consumers within the tracts being developed by Richard.

(ww) At all times material hereto, Richard had no control over any purchases of water which such consumers might make from San Gabriel.

(xx) Petitioner alleges that if the foregoing allegations set forth in paragraph 5, subparagraphs (h) and (t) above, with respect to the overstatement of long term capital gains for the taxable year 1950, together with the remaining allegations with respect to said taxable year, are determined to be correct, petitioner will be entitled to a refund with respect to said year 1950 based upon an overassessment in the amount of at least $2,425.76.

Wherefore, petitioners pray that this Court may hear the proceedings and determine that no deficiency is due from these petitioners for the taxable year 1950, but that petitioners are entitled to a refund for the amount of at least $2,425.76; and

that this Court grant such other general or special relief as may be by law provided.

/s/ JACOB SHEARER,
/s/ LEHMAN C. AARONS,
Counsel for Petitioners.

Duly Verified.

EXHIBIT "A"

Regional
1250 Subway Terminal Building
417 South Hill Street
Los Angeles 13, California
ARC-Ap:SF LA:90D:PAK

Aug. 24, 1953

Mr. Myron P. Beck
and Mrs. Ann H. Beck
Husband and Wife
c/o Mr. Ben Bisgeier
9119 Sunset Boulevard
Los Angeles 46, California

Dear Mr. and Mrs. Beck:

You are advised that the determination of your income tax liability for the taxable years ended December 31, 1949 and December 31, 1950 discloses a deficiency of $9,175.92, as shown in the statement attached.

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiencies mentioned.

Within 90 days from the date of the mailing of this letter you may file a petition with The Tax

Court of the United States, at its principal address, Washington 4, D. C., for a redetermination of the deficiency. In counting the 90 days you may not exclude any day unless the 90th day is a Saturday, Sunday, or legal holiday in the District of Columbia in which event that day is not counted as the 90th day. Otherwise Saturdays, Sundays, and legal holidays are to be counted in computing the 90-day period.

Should you not desire to file a petition, you are requested to execute, in duplicate, the enclosed form and forward it to the assistant Regional Commissioner, Appellate, 1250 Subway Terminal Building, 417 South Hill Street, Los Angeles 13, California. The signing and filing of this form will expedite the closing of your returns by permitting an early assessment of the deficiencies, and will prevent the accumulation of interest, since the interest period terminates 30 days after receipt of the form, or on the date of assessment, or on the date of payment, whichever is earlier.

Very truly yours,

T. COLEMAN ANDREWS,
Commissioner of Internal Revenue,
/s/ By W. T. TIGNOR,
Associate Chief, Appellate Division.

PaKar:vmc
Enclosures:
Statement
Form 1276
Agreement Form

Statement

ARC-Ap:SF LA:90D:PAK

Mr. Myron P. Beck and Mrs. Ann H. Beck, Husband and Wife, c/o Mr. Ben Bisgeier, 9119 Sunset Boulevard, Los Angeles 46, California.

Tax Liability for the Taxable Years ended December 31, 1949 and December 31, 1950.

Year: 1949. Income Tax Deficiency: $1,340.00.

Year: 1950. Income Tax Deficiency: $7,835.92.

Total: $9,175.92.

In making this determination of your income tax liability careful consideration has been given to the report of examination dated September 23, 1952, to your protest dated November 6, 1952, and to the statements made at a hearing held on January 27, 1953.

A copy of this letter and statement has been mailed to your representative, Mr. Jacob Shearer, 6535 Wilshire Boulevard, Los Angeles 48, California, in accordance with the authorization contained in the power of attorney executed by you.

Adjustment to Net Income

Taxable Year Ended December 31, 1949

Net income as disclosed by return	$55,660.19
Unallowable deduction:	
(a) Entertainment and promotion expense disallowed	2,456.00
Net income adjusted	$58,116.19

Explanation of Adjustment

(a) Included in the deductions claimed for entertainment and promotion expenses are items aggregating $2,456.00 which have not been substantiated as proper deductions under section 23 (a) of the Internal Revenue Code and are disallowed.

Computation of Tax

Taxable Year Ended December 31, 1949

Net income adjusted		$58,116.19
Less: Exemptions		1,200.00
Balance subject to normal tax and surtax		$56,916.19
One-half of $56,916.19		$28,458.10
Tentative surtax	$11,410.28	
Tentative normal tax	853.74	
Total tentative tax	$12,264.02	

Less: Reduction under section 12 (c) I.R.C.	1,491.68	
Total normal tax and surtax on one-half of net income		$10,772.34
Combined normal tax and surtax ($10,772.34 x 2)		$21,544.68
Correct income tax liability		$21,544.68
Income tax liability shown by return, account No. 3201028		20,204.68
Deficiency of income tax		$ 1,340.00

Adjustments to Net Income
Taxable Year Ended December 31, 1950

Net income as disclosed by return		$213,638.49
Additional income and unallowable deductions:		
(a) Long-term capital gain	12,982.93	
(b) Taxes disallowed	60.00	
(c) Promotion and entertainment expense	2,620.00	
Total		$229,301.42
Reduction:		
(d) Income from partnership	41.75	
Net income adjusted		$229,259.67

Explanation of Adjustments

(a) In your income tax return for the taxable year ended December 31, 1950 you reported capital gains from the liquidation of certain corporations. Among the assets received were valuable water contracts for which no value was reported in computing the amount of capital gain shown by your return. It is determined that the fair market value of such contracts is properly includible, under the provisions of section 117 of the Internal Revenue Code, in computing the amount of capital gain realized from the liquidation of such corporations.

It is determined that the fair market value of your share of such contracts, received by you from the corporations mentioned, are the amounts shown in the following:

Name of Corporation	Amount
Lawrence Land Co.	$7,650.98
Whittier Development Co.	5.515.80
Rex Land Co.	3,439.54
J. Richard Co.	8,854.74
Total	$25,461.06

In addition to the foregoing it is determined that you received as your distributable share of the assets of Whittier Development Co. the amount of $378.00 representing a refundable deposit and the amount of $126.80 representing your share of a claim for refund of state taxes.

Taking the foregoing into account it is determined that the correct amount of long-term capital gain realized by you during this taxable year is $184,107.55 instead of the amount, $171,-124.62, reported in your return, or an increase of $12,982.93. The amount of such increase is determined as shown in the following:

Value of water contracts	$25,461.06
Value of refundable deposit	378.00
Value of state tax claim	126.80
Total increase	$25,965.86
Long-term capital gain—50%	$12,982.93

(b) It is determined that the correct amount of the deduction for unemployment insurance is $30.00 instead of the amount, $90.00, claimed in your return, or a decrease of $60.00.

(c) Included in the deductions claimed for promotion and entertainment expenses are items aggregating $2,620.00 which have not been substantiated as proper deductions under section 23 (a) of the Internal Revenue Code and are disallowed.

(d) It is determined that the correct amount of your distributive share of the net loss of the partnership, Superior Building Co., is $193.89 instead of the amount of such loss, $152.14, reported in your return, or an increase of $41.75.

Computation of Alternative Tax
Taxable Year Ended December 31, 1950

Net income adjusted	$229,259.67
Less: Excess of net long-term capital gain over net short-term capital loss	184,107.55
Ordinary net income	$ 45,152.12
Less: Exemptions	1,200.00
Balance, subject to surtax and normal tax	$ 43,952.12

One-half of $43.952.12		$ 21,976.06
Tentative surtax	$7,707.31	
Tentative normal tax at 3%	659.28	
Total	$8,366.59	
Less reduction under Sec. 12 (c), I.R.C.	768.99	
Partial tax on one-half of net income		$ 7,597.60
Combined partial tax ($7.597.60 x 2)		$ 15.195.20
Plus: 50 per cent of $184.107.55		92,053.77
Combined alternative tax		$107,248.97

Computation of Tax
Taxable Year Ended December 31, 1950

Net income adjusted		$229,259.67
Less: Exemptions		1,200.00
Balance. subject to surtax and normal tax		$228,059.67
One-half of $228.059.67		$114,029.84
Tentative surtax	$76 385.66	
Tentative normal tax at 3%	3.420.00	
Total	$79,805.66	
Less reduction under Sec. 12 (c), I.R.C.	7,198.51	
Total normal tax and surtax on one-half of net income		$ 72,607.15
Combined normal tax and surtax ($72.607.15 x 2)		$145,214.30
Combined alternative tax		$107,248.97
Correct income tax liability		$107,248.97
Income tax liability shown on return, account No. 5—315091		99,413.05
Deficiency of income tax		$ 7,835.92

Served Nov. 13, 1953.

[Endorsed]: T.C.U.S. Filed Nov. 12, 1953.

[Title of Tax Court and Docket No. 51228.]

ANSWER

The Commissioner of Internal Revenue, by his attorney, Daniel A. Taylor, Chief Counsel, Internal Revenue Service, for answer to the petition of the above-named taxpayers, admits and denies as follows:

1, 2 and 3. Admits the allegations contained in paragraphs 1, 2 and 3 of the petition.

4. (a) to (d), inclusive. Denies the allegations of error contained in subparagraphs (a) to (d), inclusive, of paragraph 4 of the petition.

5. (a) to (e), inclusive. Admits the allegations contained in subparagraphs (a) to (e), inclusive, of paragraph 5 of the petition.

(f), (g) and (h). Denies the allegations contained in subparagraphs (f), (g) and (h) of paragraph 5 of the petition.

(i), (j) and (k). Admits the allegations contained in subparagraphs (i), (j) and (k) of paragraph 5 of the petition.

(l) and (m). Denies the allegations contained in subparagraphs (l) and (m) of paragraph 5 of the petition.

(n) to (q), inclusive. Admits the allegations contained in subparagraphs (n) to (q), inclusive, of paragraph 5 of the petition.

(r), (s) and (t). Denies the allegations contained in subparagraphs (r), (s) and (t) of paragraph 5 of the petition.

(u) to (y), inclusive. Admits the allegations contained in subparagraphs (u) to (y), inclusive, of paragraph 5 of the petition.

(z) and (aa). Denies the allegations contained in subparagraphs (z) and (aa) of paragraph 5 of the petition.

(bb) to (ee), inclusive. Admits the allegations contained in subparagraphs (bb) to (ee), inclusive, of paragraph 5 of the petition.

(ff) Denies the allegations contained in subparagraph (ff) of paragraph 5 of the petition.

(gg), (hh) and (ii). Admits the allegations contained in subparagraphs (gg), (hh) and (ii) of paragraph 5 of the petition.

(jj) and (kk). Denies the allegations contained in subparagraphs (jj) and (kk) of paragraph 5 of the petition.

(ll) to (oo), inclusive. Admits the allegations contained in subparagraphs (ll) to (oo), inclusive, of paragraph 5 of the petition.

(pp). Denies the allegations contained in subparagraph (pp) of paragraph 5 of the petition.

(qq) to (uu), inclusive. Admits the allegations contained in subparagraphs (qq) to (uu), inclusive, of paragraph 5 of the petition.

(vv), (ww) and (xx). Denies the allegations contained in subparagraphs (vv), (ww) and (xx) of paragraph 5 of the petition.

6. Denies generally and specifically each and every allegation contained in the petition not hereinbefore expressly admitted, qualified or denied.

Wherefore, it is prayed that the determination of the Commissioner be approved.

/s/ DANIEL A. TAYLOR, REM,
Chief Counsel, Internal
Revenue Service.

Of Counsel: Woolvin Patten, Acting Regional Counsel, E. C. Crouter, Associate Appellate Counsel, R. E. Maiden, Jr., Assistant Appellate Counsel, Clayton J. Burrell, Special Attorney, Internal Revenue Service.

[Endorsed]: T.C.U.S. Filed Jan. 6, 1954.

[Title of Tax Court and Docket No. 51229.]

PETITION

The above named petitioners hereby petition for a redetermination of the deficiencies set forth by the Commissioner of Internal Revenue in his Notice of Deficiency dated August 24, 1953, and as a basis of their proceedings allege as follows:

1. Petitioners are individuals whose residence is 11468 Allerton, Whittier, California. The return for the period here involved was a joint return of petitioners, as husband and wife, and was filed with the Collector of Internal Revenue for the Sixth District of California.

2. The Notice of Deficiency (a copy of which is attached and marked Exhibit "A") was mailed to petitioners on August 24, 1953.

3. The deficiency as determined by the petition was for income taxes for the year 1950 in the sum

of $1,984.73. The entire amount of said deficiency is in dispute.

4. The determination of tax set forth in the said Notice of Deficiency is based upon the following errors:

(a) Respondent erred in determining that the long term capital gains received by petitioners in respect of the liquidation of Lawrence Land Co. was understated in petitioners' Federal income tax return for said year by the sum of $1719.20, and in failing to determine that petitioners overstated their long term capital gains in respect to said liquidation by the sum of $1247.67.

(b) Respondent erred with respect to the taxable year 1950 in determining that long term capital gains received by petitioners in said year in respect of the liquidation of Whittier Development Co. were understated in petitioners' Federal income tax return for said year by $2757.90, and in failing to determine that petitioners overstated their long term capital gains in respect of said liquidation by $1732.35.

5. The facts upon which petitioners rely as a basis for this proceeding, are as follows:

(a) All of the transactions here involved were those of petitioner, Milton Gersten, as the managing spouse of the community property of the parties, and for convenience the term "petitioner" as hereinafter used in this paragraph will refer to petitioner, Milton Gersten.

(b) On or about May 26, 1949 petitioner purchased for the sum of $1500. a total of 15 shares of the stock of Lawrence Land Co. (hereinafter referred to as "Lawrence"). Said 15 shares represented 10% of all of the stock of Lawrence issued and outstanding at all times material hereto.

(c) Lawrence was a corporation incorporated pursuant to the laws of the State of California on or about March 25, 1949, and on that date commenced to do business within the State of California.

(d) Lawrence's business consisted of the subdivision of unimproved land into residential lots, including the installation of subdivision improvements, the erection of residences or homes upon such lots, and the sale thereof.

(e) On December 31, 1950, Lawrence was finally wound up and dissolved, and on or about said date its assets were distributed to its stockholders proportionately to their stock holdings.

(f) Pursuant to the winding up and complete liquidation of Lawrence petitioner received as his proportion of the assets of Lawrence the sum of $19,595.60 in cash, and an undivided 10% interest in certain real property in the County of Los Angeles, State of California, which undivided interest had a then fair market value of $7,460.00. There was also assigned to petitioner, in connection with said liquidation a 10% interest in a certain contract, dated January 25, 1950, as amended February 9, 1950, between Lawrence and San Gabriel Valley

Water Company (hereinafter referred to as "San Gabriel").

(g) In connection with the dissolution of Lawrence, petitioner and the other stockholders of Lawrence entered into a written agreement on December 26, 1950, in which said stockholders assumed and became responsible for all of the debts, obligations and liabilities of Lawrence. Said agreement was entered into in order to comply with sections 5000 and 5001 of the Corporations Code of the State of California pertaining to voluntary dissolutions of corporations.

(h) The undisputed amount of Lawrence's liability under the Excess Profits Tax Act of 1950, as amended, as of the time of its dissolution, was $12,476.68, and petitioner's obligation in respect thereof, pursuant to his assumption of liability under the agreement referred to in paragraph 5 (g) above, amounted to $1,247.67. Petitioner's accountant, at the time he prepared Petitioner's 1950 Federal income tax return, failed to take into account said sum of $1,247.67 so assumed by petitioner and accordingly, overstated petitioner's long term capital gains in respect of the dissolution of Lawrence by the sum of $1,247.67.

(i) At all times material hereto San Gabriel was engaged in the business of supplying water to residences and other properties located in the district in which the tract of real property of Lawrence was situated.

(j) Pursuant to said contract, San Gabriel

agreed to extend its pipelines for the servicing of water to Lawrence's property upon payment to it by Lawrence of the sum of $31,021.00.

(k) Said contract further provided for contingent refunds to Lawrence by San Gabriel of all, or a portion, of the said sum of $31,021.00 up to the whole thereof.

(l) By the terms of said contract, the aggregate amount of such refunds, if any, was dependent upon the amount of gross revenue, if any, which San Gabriel might receive, within a limited period of time, from the sale of water to consumers within the tract being developed by Lawrence.

(m) At all times material hereto, neither Lawrence nor San Gabriel had any control over any purchases of water which such consumers might make from San Gabriel.

(n) On or about the month of May, 1949, petitioner purchased 200 shares of stock of Whittier Development Co. (hereinafter referred to as "Whittier") for the sum of $2,000.00 and thereafter and until the dissolution of Whittier owned said 200 shares. Said 200 shares represented 20% of all of the stock of Whittier issued and outstanding at all times material hereto.

(o) Whittier was a corporation incorporated pursuant to the laws of the State of California on or about August 20, 1948, and during the month of July of 1949 commenced to do business within the State of California.

(p) Whittier's business consisted of the subdivi-

sion of unimproved land into residential lots, including the installation of subdivision improvements, the erection of residences or homes upon such lots, and the sale thereof.

(q) On December 28, 1950, Whittier was finally wound up and dissolved, and on or about said date, its assets were distributed to its stockholders proportionately to their stock holdings.

(r) Pursuant to the winding up and complete liquidation of Whittier petitioner received as his proportion of the assets of Whittier the sum of $38,589.13 in cash. There was also assigned to petitioner, in connection with said liquidation, a 20% interest in a certain contract, dated November 29, 1949, between Whittier and San Gabriel, and a 20% interest in a certain contract, dated March 10, 1950, between Whittier and San Gabriel.

(s) In connection with the dissolution of Whittier, petitioner and the other stockholders of Whittier entered into a written agreement on December 16, 1950, in which said stockholders assumed and became responsible for all of the debts, obligations and liabilities of Whittier. Said agreement was entered into in order to comply with sections 5000 and 5001 of the Corporations Code of the State of California pertaining to voluntary dissolutions of corporations.

(t) The undisputed amount of Whittier's liability under the Excess Profits Tax Act of 1950, as amended, as of the time of its dissolution, was $8,661.79, and petitioner's obligation in respect

thereof, pursuant to his assumption of liability under the agreement referred to in paragraph 5 (s) above, amounted to $1,732.35. Petitioner's accountant, at the time he prepared petitioner's 1950 Federal income tax return, failed to take into account said sum of $1,732.35 so assumed by petitioner and accordingly, overstated petitioner's long term capital gain in respect of the dissolution of Whittier by the sum of $1,732.35.

(u) At all times material hereto San Gabriel was engaged in the business of supplying water to residences and other properties located in the district in which the tracts of real property of Whittier were situated.

(v) Pursuant to the contract dated November 29, 1949, San Gabriel agreed to extend its pipelines for the servicing of water to one of the tracts being developed by Whittier upon the payment to it by Whittier of the sum of $23,841.00.

(w) In said contract it further provided for contingent refunds to Whittier by San Gabriel of all, or a portion, of the said sum of $23,841.00.

(x) Pursuant to the contract dated March 10, 1950, San Gabriel agreed to extend its pipelines for the servicing of water to another of the tracts being developed by Whittier upon payment to it by Whittier of the sum of $5,214.00.

(y) Said contract further provided for contingent refunds to Whittier by San Gabriel of all, or a portion, of the said sum of $5,214.00.

(z) By the terms of said contracts, the aggregate amounts of such refunds, if any, were dependent upon the amount of gross revenue, if any, which San Gabriel might receive, within a limited period of time, from the sale of water to consumers within the tracts being developed by Whittier.

(aa) At all times material hereto, Whittier had no control over any purchases of water which such consumers might make from San Gabriel.

(bb) Petitioner alleges that if the foregoing allegations set forth in paragraph 5, subparagraphs (h) and (t) above, with respect to the overstatement of long term capital gains for the taxable year 1950, together with the remaining allegations with respect to said taxable year, are determined to be correct, petitioners will be entitled to a refund with respect to said year based upon an overassessment in the amount of at least $745.00.

Wherefore, petitioners pray that this Court may hear the proceedings and determine that no deficiency is due from these petitioners for the taxable year 1950, but that petitioners are entitled to a refund for the said taxable year based upon an overassessment in the amount of at least $745.00; and that this Court grant such other general or special relief as may be by law provided.

/s/ JACOB SHEARER,
/s/ LEHMAN C. AARONS,
Counsel for Petitioner.

Duly Verified.

EXHIBIT "A"

Regional
1250 Subway Terminal Building
417 South Hill Street
Los Angeles 13, California
ARC-Ap:SF LA:90D:PAK

Aug. 24, 1953

Mr. Milton Gersten
and Mrs. Mary Gersten
Husband and Wife
11468 Allerton
Whittier, California

Dear Mr. and Mrs. Gersten:

You are advised that the determination of your income tax liability for the taxable year ended December 31, 1950 discloses a deficiency of $1,984.73, as shown in the statement attached.

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiency mentioned.

Within 90 days from the date of the mailing of this letter you may file a petition with The Tax Court of the United States, at its principal address, Washington 4, D. C., for a redetermination of the deficiency. In counting the 90 days you may not exclude any day unless the 90th day is a Saturday, Sunday, or legal holiday in the District of Columbia, in which event that day is not counted as the 90th day. Otherwise, Saturdays, Sundays, and legal holidays are to be counted in computing the 90-day period.

Should you not desire to file a petition, you are requested to execute, in duplicate, the enclosed form and forward it to the Assistant Regional Commissioner, Appellate, 1250 Subway Terminal Building, 417 South Hill Street, Los Angeles 13, California. The signing and filing of this form will expedite the closing of your return by permitting an early assessment of the deficiency, and will prevent the accumulation of interest, since the interest period terminates 30 days after receipt of the form, or on the date of assessment, or on the date of payment, whichever is earlier.

Very truly yours,

T. COLEMAN ANDREWS,
Commissioner of Internal Revenue,

/s/ By W. T. TIGNOR,
Associate Chief, Appellate Division.

PAKar:lee
Enclosures:
Statement
Form 1276
Agreement Form

Statement

ARC-Ap:SF LA:90D:PAK

Mr. Milton Gersten and Mrs. Mary Gersten, Husband and Wife, 11468 Allerton, Whittier, California.

Tax Liability for the Taxable Year Ended December 31, 1950.
Year: 1950. Income Tax Deficiency: $1,934.73.

In making this determination of your income tax liability careful consideration has been given to the report of examination

dated September 23, 1952, to your protest dated November 6, 1952, and to the statements made at a hearing held on January 27, 1953.

A copy of this letter and statement has been mailed to your representative, Mr. Jacob Shearer, 6535 Wilshire Boulevard, Los Angeles 48, California, in accordance with the authorization contained in the power of attorney executed by you.

Adjustments to Net Income
Taxable Year Ended December 31, 1950

Net income as disclosed by return	$81,634.10
Additional income and unallowable deductions:	
(a) Long-term capital gain	2,238.55
(b) Taxes disallowed	15.00
(c) Entertainment expense disallowed	1,596.95
Net income adjusted	$85,484.60

Explanation of Adjustments

(a) In your income tax return for the taxable year ended December 31, 1950, you reported capital gains from the liquidation of certain corporations. Among the assets received were valuable water contracts for which no value was reported in computing the amount of capital gain shown by your return. It is determined that the fair market value of such contracts is properly includible, under the provisions of Section 117 of the Internal Revenue Code, in computing the amount of capital gain realized from the liquidation of such corporations.

It is determined that the fair market value of your share of such contracts, received by you from the corporations mentioned, are the amounts shown in the following:

Name of Corporation	Amount
Lawrence Land Co.	$1,530.20
Whittier Development Co.	2,757.90
Total	$4,288.10

It is also determined that you received the amount of $189.00 as your distributive share of a refundable deposit with Southern California Edison Company upon the liquidation of Whittier Development Co., which amount was not reported in your return.

Taking the foregoing into account the increase in the amount of long-term capital gain realized during this taxable year is determined as shown in the following:

Increases:		
Value of water contracts	$4,288.10	
Value of refundable deposit	189.00	
Total	$4,477.10	
Increase of long-term capital gain (50% of $4,477.10)		$2,238.55

(b) It is determined that the correct deduction for social security taxes is the amount of $30.00 instead of the amount, $45.00, claimed in your return or a decrease of $15.00.

(c) Included in the deduction claimed for entertainment expense are items aggregating $1,596.95 which have not been substantiated as proper deductions under Section 23(a) of the Internal Revenue Code and are disallowed.

Computation of Alternative Tax
Taxable Year Ended December 31, 1950

Net income adjusted		$85,484.60
Less: Excess of net long-term capital gain over net short-term capital loss		33,262.96
Ordinary net income		$52,221.64
Less: Exemptions		3,000.00
Balance, subject to surtax and normal tax		$49,221.64
One-half of $49,191.64		
Tentative surtax	$9,182.06	
Tentative normal tax at 3%	738.32	
Total	$9,920.38	
Less reduction under Sec. 12 (c), I.R.C.	908.83	
Partial tax on one-half of net income		$ 9,011.55
Combined partial tax ($9,011.55 x 2)		$18,023.10
Plus: 50 per cent of $33,262.96		16,631.48
Combined alternative tax		$34,654.58

Computation of Tax
Taxable Year Ended December 31, 1950

Net income adjusted		$85,484.60
Less: Exemptions		3,000.00
Balance, subject to surtax and normal tax		$82,484.60
One-half of $82,484.60		$41,242.30
Tentative surtax	$19,359.92	
Tentative normal tax at 3%	1,237.27	
Total	$20,597.19	
Less reduction under Sec. 12 (c), I.R.C.	1,869.75	
Total normal tax and surtax on one-half of net income		$18,727.44
Combined normal tax and surtax ($18,727.44 x 2)		$37,454.88
Combined alternative tax		$34,654.58
Correct income tax liability		$34,654.58
Income tax liability shown on return, account No. 3251339		32,669.85
Deficiency of income tax		$ 1,984.73

Served Nov. 13, 1953.

[Endorsed]: T.C.U.S. Filed Nov. 12, 1953.

[Title of Tax Court and Docket No. 51229.]

ANSWER

The Commissioner of Internal Revenue, by his attorney, Daniel A. Taylor, Chief Counsel, Internal Revenue Service, for answer to the petition of the above-named taxpayers, admits and denies as follows:

1, 2 and 3. Admits the allegations contained in paragraphs 1, 2 and 3 of the petition.

4. (a) and (b). Denies the allegations of error

contained in subparagraphs (a) and (b) of paragraph 4 of the petition.

5. (a) to (e), inclusive. Admits the allegations contained in subparagraphs (a) to (e), inclusive, of paragraph 5 of the petition.

(f), (g) and (h). Denies the allegations contained in subparagraphs (f), (g) and (h) of paragraph 5 of the petition.

(i), (j) and (k). Admits the allegations contained in subparagraphs (i), (j) and (k) of paragraph 5 of the petition.

(l) and (m). Denies the allegations contained in subparagraphs (l) and (m) of paragraph 5 of the petition.

(n) to (q), inclusive. Admits the allegations contained in subparagraphs (n) to (q), inclusive, of paragraph 5 of the petition.

(r), (s) and (t). Denies the allegations contained in subparagraphs (r), (s) and (t) of paragraph 5 of the petition.

(u) to (y), inclusive. Admits the allegations contained in subparagraphs (u) to (y), inclusive, of paragraph 5 of the petition.

(z), (aa) and (bb). Denies the allegations contained in subparagraphs (z), (aa) and (bb) of paragraph 5 of the petition.

6. Denies generally and specifically each and every allegation contained in the petition not hereinbefore expressly admitted, qualified or denied.

Wherefore, it is prayed that the determination of the Commissioner be approved.

/s/ DANIEL A. TAYLOR, REM,
Chief Counsel, Internal
Revenue Service.

Of Counsel: Woolvin Patten, Acting Regional Counsel, E. C. Crouter, Associate Appellate Counsel, R. E. Maiden, Jr., Assistant Appellate Counsel, Clayton J. Burrell, Special Attorney, Internal Revenue Service.

[Endorsed]: T.C.U.S. Filed Jan. 6, 1954.

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28 T. C. No. 84

Tax Court of the United States

Docket Nos. 51226-51242

Albert Gersten, et al.,[1] Petitioners, v. Commissioner of Internal Revenue, Respondent.

Filed June 28, 1957

FINDINGS OF FACT AND OPINION

1. Four corporations in which certain of the petitioners were stockholders were engaged in the business of subdividing tracts of land into lots and constructing and selling houses thereon. To procure the waterlines necessary to supply water for the houses so built and sold, the corporations, under

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[1] Proceedings of the following petitioners are considered herewith: Albert Gersten and Lucille Gersten, Docket No. 51227; Myron P. Beck and Ann H.

contracts with the water company, paid the cost of the extension of the water company's lines into the various properties. For a period of ten years from the date of completion of the waterlines, the water company agreed to make payments to the corporations based on a percentage of the gross revenue it would derive from the sale of water to the occupants of the houses sold, but in an amount not to exceed cost to the corporations for the running of the waterlines. All of the houses were completed and sold, and the four corporations distributed in dissolution the water company contracts to their stockholders. In reporting their gain upon the sales of the houses, the four corporations treated the cost

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Beck, Docket No. 51228; Milton Gersten and Mary Gersten, Docket No. 51229; Rex Land Co., a dissolved corporation, Docket No. 51230; Albert Gersten, alleged Transferee of Rex Land Co., Docket No. 51231; Myron P. Beck and Ann H. Beck, alleged Transferees of Rex Land Co., Docket No. 51232; Lawrence Land Co., a dissolved corporation, Docket No. 51233; Albert Gersten, alleged Transferee of Lawrence Land Co., Docket No. 51234; Myron P. Beck and Ann H. Beck, alleged Transferees of Lawrence Land Co., Docket No. 51235; Milton Gersten and Mary Gersten, alleged Transferees of Lawrence Land Co., Docket No. 51236; Albert Gersten, alleged Transferee of J. Richard Co., Docket No. 51237; Myron P. Beck and Ann H. Beck, alleged Transferees of J. Richard Co., Docket No. 51238; Whittier Development Co., a dissolved corporation, Docket No. 51239; Albert Gersten, alleged Transferee of Whittier Development Co., Docket No. 51240; Myron P. Beck and Ann H. Beck, alleged Transferees of Whittier Development Co., Docket No. 51241; and Milton Gersten and Mary Gersten, alleged Transferees of Whittier Development Co., Docket No. 51242.

to them of the waterlines as part of the cost of the houses sold, which treatment was disallowed by the respondent in the determinations herein. The stockholders, in reporting their gain upon dissolution of the corporations, attributed no value to the water company contracts distributed to them. The respondent determined that each of the contracts had a fair market value at the time of distribution and the amount thereof, and took such fair market value into account in determining the gain to the stockholders from the dissolution of the corporations. Held, that payments made by the corporations to the water company for the construction of the waterlines were properly included by corporations in computing the cost of the houses sold. Colony, Inc., 26 T. C. 30. Held, further, that at the time of distribution each of the water company contracts had a fair market value equal, at least, to the amount determined by the respondent, and the respondent properly took such fair market value into account in determining the gain realized by the stockholders upon receipt of the contracts.

2. Petitioner Albert Gersten and one Robbins had been the owners, in equal part, of the stock of a corporation, the assets of which they had received in equal shares upon its dissolution, and by reason thereof, Gersten and Robbins became liable as transferees of the said corporation for $44,721.60 in Federal taxes and interest thereon. In December 1947, Gersten paid $40,000 of the said sum and on April 5, 1949, paid the remaining $4,721.60, of which $1,261.13 represented interest. At the time of

the final payment in April of 1949, Robbins was insolvent, and Gersten in his 1949 return deducted the entire $4,721.60. The respondent in his determination of deficiency determined that the $4,721.60 paid by Gersten was paid one-half on his own account and one-half on Robbins' account, that the $2,360.80 paid on Robbins' account was a nonbusiness bad debt, deductible as a short-term capital loss under section 23 (k) of the Code, that of the $2,360.80 paid on his own account, $630.57 was interest and deductible as such, and the remaining $1,730.23 was a long-term capital loss. Under authority of Putnam v. Commissioner, 352 U. S. 82, and Arrowsmith v. Commissioner, 344 U. S. 47, the respondent's determination is sustained.

3. On April 3, 1950, petitioner Lucille Gersten obtained a California interlocutory decree of divorce from petitioner Albert Gersten, which, under California law, did not become a final decree until April 3, 1951. On November 2, 1950, Albert Gersten obtained a final decree of divorce in Mexico and on that date married Bernice Ann Gersten in Mexico. He and Bernice filed a joint return for 1950; respondent determined they were not entitled to do so. Albert and Bernice Ann Gersten were at all times residents of California. Held, petitioner Albert Gersten and Bernice Ann Gersten were not entitled to file a joint return of income for 1950.

4. J. Richard Company, a California corporation incorporated on July 10, 1947, was engaged in the business of purchasing tracts of land which it subdivided into lots on which it constructed and

sold houses. It dissolved on June 22, 1950. Lawrence Land Company was a California corporation incorporated on March 25, 1949. It dissolved on December 31, 1950. It also was engaged in the business of acquiring tracts of land which it subdivided into lots on which it constructed and sold houses. Petitioners Albert Gersten and Myron P. Beck owned all of the stock of J. Richard Company. They and Milton Gersten owned all of the stock of Lawrence Land Company. Held, the business of J. Richard Company was substantially similar to the trade or business engaged in by Lawrence Land Company during 1950, within the meaning of section 430 (e) (2) (B) (ii) of the 1939 Code, and Lawrence Land Company was therefore in its fourth taxable year for purposes of such section in computing its excess profits tax liability for the fiscal period March 1, 1950 to December 31, 1950.

Jacob Shearer, Esq., for the petitioners.
George E. Constable, Esq., for the respondent.

The respondent determined income tax and transferee liability deficiencies against the petitioners herein as follows:

Docket No.	Petitioner	Taxable Year or Period	Deficiency
51226	Albert Gersten	1950	$10,429.15
51227	Albert Gersten and Lucille Gersten	1949	1,687.02
51228	Myron P. Beck and Ann H. Beck	1949	1,340.00
		1950	7,835.92
51229	Milton Gersten and Mary Gersten	1950	1,984.73

Docket No.	Petitioner	Taxable Year or Period	Deficiency
51230	Rex Land Co., a dissolved corporation	Yr. ended 1/31/50	6,568.55
		2/1/50—10/25/50	1,104.16
51231	Albert Gersten, transferee of Rex Land Co.	Yr. ended 1/31/50	6,568.55
		2/1/50—10/25/50	1,104.16
51232	Myron P. Beck and Ann H. Beck, transferees of Rex Land Co.	Yr. ended 1/31/50	6,568.55
		2/1/50—10/25/50	1,104.16
51233	Lawrence Land Co., a dissolved corporation	3/1/50—12/31/50	10,908.88[2]
51234	Albert Gersten, transferee of Lawrence Land Co.	3/1/50—12/31/50	10,908.88
51235	Myron P. Beck and Ann H. Beck, transferees of Lawrence Land Co.	3/1/50—12/31/50	10,908.88
51236	Milton Gersten and Mary Gersten, transferees of Lawrence Land Co.	3/1/50—12/31/50	10,908.88
51237	Albert Gersten, transferee of J. Richard Co.	Yr. ended 6/30/49	10,886.75
		Yr. ended 6/30/50	5,306.59
51238	Myron P. Beck and Ann H. Beck, transferees of J. Richard Co.	Yr. ended 6/30/49	$10,886.75
		Yr. ended 6/30/50	5,306.59
51239	Whittier Development Co., a dissolved corporation	Yr. ended 2/28/50	7,503.64

[2] Such amount is the determined net deficiency in income tax imposed by sections 13 and 15 of chapter I, the gross deficiency in such tax of $15,202.94 being offset by an overpayment of excess profits tax imposed by section 430 of such chapter in the amount of $4,294.06. Union Telephone Co., 41 B.T.A. 152; cf. Will County Title Co., 38 B.T.A. 1396; Rowan Cotton Mills Co., 1 T. C. 865, affd. 140 F. 2d 277, certiorari denied 322 U. S. 740; Pioneer Parachute Co., 4 T. C. 27; Difco Laboratories, Inc., 10 T. C. 660.

Docket No.	Petitioner	Taxable Year or Period	Deficiency
51240	Albert Gersten, transferee of Whittier Development Co.	Yr. ended 2/28/50	7,503.64
51241	Myron P. Beck and Ann H. Beck, transferees of Whittier Development Co.	Yr. ended 2/28/50	7,503.64
51242	Milton Gersten and Mary Gersten, transferees of Whittier Development Co.	Yr. ended 2/28/50	7,503.64

The petitioner transferees have conceded their liability as transferees in the amount of any deficiencies determined herein against the corporate petitioners in Docket Nos. 51230, 51233, and 51239. Petitioners Albert Gersten and Myron P. Beck have also conceded their transferee liability, determined in Docket Nos. 51237 and 51238, for such additional taxes as J. Richard Company, which is not a petitioner, should have been liable for, as may be determined herein. The parties agree that Ann H. Beck, the wife of Myron P. Beck and a petitioner in Docket Nos. 51232, 51235, 51238, and 51241, is not liable as a transferee of the corporate petitioners or of J. Richard Company.

The issues to be decided are (1) whether the corporate petitioners and another corporation, J. Richard Company, properly included payments to a water company for extending pipelines to certain subdivisions developed by them, in computing the cost of property sold, when such payments were repayable upon the happening of certain contingencies; (2) what value, if any, was attributable to the

said repayment rights in determining the gain realized by the stockholders upon distributions to them in liquidation of the said corporations; (3) whether a payment in 1949 by petitioner Albert Gersten, in final satisfaction of the Federal income tax liability of a dissolved corporation, half of whose assets he had received upon dissolution, resulted in a fully deductible loss under section 23 (e) (2) of the Internal Revenue Code of 1939; (4) whether petitioner Albert Gersten and his alleged wife, Bernice Anne Gersten, were entitled to file a joint Federal income tax return for the year 1950; and (5) whether the business of J. Richard Company was "substantially similar to the trade or business" engaged in by petitioner Lawrence Land Company during the year 1950, within the meaning of section 430 (e) (2) (B) (ii).[3]

Findings of Fact

Some of the facts have been stipulated and are found as stipulated.

During the years in issue, petitioners Albert Gersten and his wife, Lucille Gersten,[4] and Myron P. Beck and his wife, Ann H. Beck, were residents of Los Angeles, California. Petitioners Milton Gersten and his wife, Mary Gersten, were residents of

[3] See footnote 2, supra.

[4] Lucille Gersten secured an interlocutory decree of divorce in California from Albert Gersten on April 3, 1950. Albert Gersten secured a final decree of divorce from a Mexican court on November 2, 1950, and on that day, in Mexico, married Bernice Anne Gersten with whom he filed a joint return for 1950.

Whittier, California. All of the individual petitioners kept their books and reported their income on a cash basis. The corporate petitioners and another corporation, J. Richard Company, kept their books and filed their returns on an accrual basis. The returns of all petitioners and those of J. Richard Company were filed with the former collector of internal revenue for the sixth district of California.

From July 1947 until the end of 1950, petitioners Albert Gersten and Myron P. Beck were the controlling stockholders of four corporations which were engaged in the business of subdividing tracts of land, constructing houses thereon, and selling such houses. Petitioner Milton Gersten was a stockholder in two of such corporations.

The extension of pipelines for water service was essential to the subdivision of the tracts and the sale of the houses constructed thereon. In order to provide water facilities for the subdivisions, contracts were entered into with the San Gabriel Valley Water Company, hereinafter referred to as San Gabriel, which agreed to extend its waterlines into the subdivisions in question, conditioned, however, upon payment by the subdividing corporations of the cost of such extensions. San Gabriel was a California water utility corporation, subject to the jurisdiction of the Public Utilities Commission of the State of California. It held a franchise to operate in the area in which the tracts in question were located. The minimum rate for water which San Gabriel charged during 1948, 1949, and 1950 was $1.25 per month.

Under the contracts, San Gabriel was to make payments to the subdividing corporations on the basis of its gross receipts from the sale of water to homes in the particular subdivision. The payments were to be made for a period of ten years from the date the lines were completed, unless the full amount should be paid prior to the end of such ten-year period, and a subdividing corporation might or might not receive repayment in full. The corporations did not hold title to the facilities.

The four corporations were all dissolved by December 31, 1950. Substantial amounts of their payments to San Gabriel remained unpaid at the time of their dissolution, and such contracts, which were fully transferable, were assigned to their stockholders. Similar contracts to those here in issue were bought and sold, and, under normal conditions, approximately 70 per cent of the original payment might be expected on such contracts. Some of the conditions which affected the amount which might be refunded were: (1) the time in which all houses within a subdivision were completed; (2) the time within which the houses, once completed, were sold and occupied; and (3) the amount of water the consumers used, which in turn was dependent on such factors as the number of water-consuming appliances owned by them, weather conditions during the year, and the amount of plantings and vegetation needing irrigation.

In computing its gain for income tax purposes, each of the four corporations included the payments made to San Gabriel in arriving at the cost

of the houses sold. The respondent determined that such payments should not have been so included.

Upon the dissolution of the corporations, Albert Gersten, Myron P. Beck, and Milton Gerston received all corporate assets, including the water contracts. They did not assign any value to their respective interests in such contracts, in arriving at the gain realized upon liquidation of the corporations. The respondent determined that each of the contracts did have a fair market value when they were received by the stockholders in liquidation, and on the basis thereof increased the amount of capital gain realized in his determination of deficiencies herein. Details of the contract which each corporation entered into with San Gabriel, and the manner in which such contracts were treated for tax purposes by both the corporations and the transferees of corporate assets, were as follows:

J. Richard Company. J. Richard Company, hereinafter referred to as Richard, was a California corporation, incorporated on July 10, 1947, and dissolved on or about June 22, 1950. Richard's stock was owned equally by Albert Gersten and Myron P. Beck. During the course of its existence, Richard acquired three tracts of land which it subdivided into lots on which it constructed and sold houses. On December 3, 1947, petitioner Albert Gersten, on behalf of Richard, entered into a contract with San Gabriel providing for the installation of waterlines to two of the three tracts. San Gabriel completed the installation of the waterlines on April 2, 1948. The contract provided for a payment to San Ga-

briel of $23,764, which sum was paid to it by Richard on or about the date on which the contract was entered into. San Gabriel agreed to repay such payment "in the amount of ⅓ of the gross revenues derived from sale of water to occupants of said subdivisions for a period not to exceed 10 years from date hereof."

On December 2, 1948, petitioner Albert Gersten, on behalf of Richard, entered into a similar contract with San Gabriel to provide water facilities for the third tract. The contract provided for the payment of $15,258, which amount was paid to San Gabriel by Richard on or about December 2, 1948. San Gabriel agreed to repay such payment in the amount of one-third of the gross revenue derived from the sale of water for a period not exceeding ten years from the date of the contract.

At the time of Richard's dissolution, on June 22, 1950, San Gabriel had repaid $2,325.37 on the contract covering the first two tracts, and $1,277.69 on the contract covering the third tract. All of the houses constructed by Richard on the first two tracts had been sold by June 1, 1949, and all of the houses constructed by it on the third tract had been sold by February 3, 1950.

On its income tax return for the fiscal year ended June 30, 1949, Richard included $24,735.99 of its payments to San Gabriel in computing the total cost of houses sold by it during such year. On its return for the fiscal year ended June 30, 1950, it included $11,149.22 of the payments made to San Gabriel in computing the cost of houses sold by it

during that year. In determining deficiencies against Albert Gersten and Myron P. Beck, as transferees of Richard for such years, the respondent disallowed the inclusion by Richard of payments to San Gabriel for the installation of water facilities, as being a part of the cost of houses sold by it.

Upon the dissolution of Richard on June 22, 1950, petitioners Albert Gersten and Myron P. Beck were each paid cash in the amount of $38,202.12, and received a 50 per cent interest in Richard's contracts with San Gabriel. They did not assign any value to the interest received in such contracts in computing the amount of capital gain realized on the dissolution of Richard. Respondent determined that such contracts had a fair market value of 50 per cent of the amount which remained unpaid on June 22, 1950, or $17,709.48, and accordingly increased the amount of capital gain realized by Gersten and Beck on Richard's distribution of its assets to them.

The contracts had a fair market value at the time of Richard's dissolution, equal, at least, to the amount determined by the respondent.

Whittier Development Company. Whittier Development Company, hereinafter referred to as Whittier, was a California corporation, incorporated on August 20, 1948, and dissolved on or about December 28, 1950. From February 28, 1950 to December 28, 1950, its stock was owned as follows:

Albert Gersten	40 Per cent
Myron P. Beck	40 " "
Milton Gersten	20 " "

During the course of its existence, Whittier acquired two parcels of land which it subdivided into lots on which it constructed and sold houses. In order to provide water facilities for such tracts, it entered into two contracts with San Gabriel. The first was dated November 29, 1949. Whittier agreed to and did pay, on or about that date, the sum of $23,841 to San Gabriel. San Gabriel agreed to repay such payment within ten years from the date of the contract by payment of 35 per cent of the annual gross revenues derived from the sale of water. On March 10, 1950, Whittier entered into a second contract with San Gabriel providing for the installation of water facilities to the other tract which it owned. It paid San Gabriel the sum of $5,214. San Gabriel agreed to repay such sum within a ten-year period from completion of the installation of the facilities. Such repayment was to be made from 35 per cent of the gross revenues derived by it from the sale of water. Installation of the facilities was completed by April 14, 1950. By December 28, 1950, San Gabriel had repaid $1,413.02 on the first contract and $62.98 on the second. Whittier had sold all houses on the first tract by June 7, 1950, and on the second tract by December 15, 1950.

On the return which Whittier filed for the fiscal year ended February 28, 1950, it included $14,253.67 of the amount paid to San Gabriel under the first contract as a part of the cost of houses sold during such taxable year. In determining the deficiencies herein, the respondent disallowed the in-

clusion of such sum as a part of the cost of houses sold by Whittier.[5]

Upon the dissolution of Whittier on December 28, 1950, petitioners Albert Gersten and Myron P. Beck each received the sum of $77,160.26 and a 40 per cent interest in each of Whittier's contracts with San Gabriel. Petitioner Milton Gersten received the sum of $38,580.13 and a 20 per cent interest in each of the contracts with San Gabriel. Albert Gersten, Beck, and Milton Gersten did not assign any value to the interest received in such contracts in computing the amount of capital gain realized on the dissolution of Whittier. Respondent determined that such contracts had a fair market value of 50 per cent of the amount which remained unpaid on December 28, 1950, or $14,545.50, and accordingly increased the amount of capital gain realized by Albert Gersten, Beck, and Milton Gersten on Whittier's distribution of its assets to them. Such contracts had a fair market value at the time of Whittier's dissolution, equal, at least, to the amount determined by the respondent.

Rex Land Company. Rex Land Company, hereinafter referred to as Rex, was a California corporation, incorporated on February 4, 1949, and dissolved on or about October 25, 1950. Its stock was equally owned by petitioners Albert Gersten and

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[5] The amount of the payments to San Gabriel included by Whittier in computing the cost of houses sold during the fiscal period March 1, 1950 to December 28, 1950, is not in issue, since respondent determined an overpayment of tax for such period.

Myron P. Beck. Rex acquired a tract of land which it subdivided into lots on which it constructed and sold houses. On February 9, 1949, it entered into a contract with San Gabriel for the installation of waterlines to the tract. For the installation of such facilities, Rex agreed to and did pay to San Gabriel the sum of $14,707.20. San Gabriel agreed to repay such payment within a ten-year period from the date on which installation of the facilities was completed, which was April 22, 1949. Such repayment was to be made from 35 per cent of the gross revenues derived by it from the sale of water. By October 25, 1950, San Gabriel had repaid $949.02 of such sum. All of the houses constructed on the tract were sold by March 16, 1950.

On its income tax return for the period February 4, 1949 to January 31, 1950, Rex included $12,658.61 of the amount paid to San Gabriel as a part of the cost of houses sold by it during such period. On its return for the fiscal period ended October 25, 1950, it included $1,265.12 of such payment as a part of the cost of houses sold by it during such period. In determining the deficiencies herein, respondent disallowed the inclusion of such sums as a part of the cost of the houses sold.

Upon the dissolution of Rex on October 25, 1950, petitioners Albert Gersten and Myron P. Beck each received the sum of $1,158.84 in cash, a 50 per cent interest in certain real property having a fair market value of $215,350, and a 50 per cent interest in Rex's contract with San Gabriel. Gersten and Beck did not assign any value to the interest received in

such contract in computing the amount of capital gain realized on the dissolution of Rex. Respondent determined that the contract had a fair market value of 50 per cent of the amount which remained unpaid on October 25, 1950, or $7,132.68, and accordingly increased the amount of capital gain realized by them on Rex's distribution of its assets to them. Such contract had a fair market value at the time of Rex's dissolution, equal, at least, to the amount determined by the respondent.

Lawrence Land Company. Lawrence Land Company, hereinafter referred to as Lawrence, was a California corporation, incorporated on March 25, 1949, and dissolved on or about December 31, 1950. The stock of the corporation was owned as follows:

Albert Gersten	40 Per cent
Myron P. Beck	50 " "
Milton Gersten	10 " "

Lawrence acquired a parcel of land which it subdivided into lots on which it constructed and sold houses. On January 26, 1950, it entered into a contract with San Gabriel for the installation of waterlines to the tract. Such contract was modified by a subsequent contract entered into on February 14, 1950. Under the contract, as modified, Lawrence agreed to and did pay to San Gabriel the sum of $31,021. San Gabriel agreed to repay such sum within a ten-year period from the date on which installation of the facilities was completed, which was March 29, 1950. Such repayment was to be made from 35 per cent of the gross revenue received from the sale of water to consumers. All of

the houses which Lawrence constructed on the tract were completed and sold by December 11, 1950. On its return for the fiscal period March 1, 1950 to December 31, 1950, Lawrence included the sum of $31,021 paid to San Gabriel as a part of the cost of the houses sold. In determining the deficiencies herein, respondent disallowed the inclusion of the payment to San Gabriel. No repayments were paid by San Gabriel to Lawrence prior to Lawrence's dissolution on December 31, 1950; but payments commenced to be made on March 1, 1951. On December 31, 1950, Lawrence distributed to petitioner Albert Gersten the sum of $78,382.40, and an undivided 40 per cent interest in certain real property, which interest had a fair market value of $29,840, and a 40 per cent interest in the contract, as modified, with San Gabriel. It distributed to petitioner Myron P. Beck cash in the amount of $97,978, a 50 per cent interest in certain real property, which interest had a fair market value of $37,300, and a 50 per cent interest in Lawrence's contract with San Gabriel. It distributed to petitioner Milton Gersten the sum of $19,595.59, a 10 per cent interest in certain real property, which interest had a fair market value of $7,460, and a 10 per cent interest in the contract with San Gabriel. Albert Gersten, Beck, and Milton Gersten did not assign any value to the interest received in such contract in computing the amount of capital gain realized on the dissolution of Lawrence. Respondent determined that the contract had a fair market value of $15,301.96 on December 31, 1950, and accordingly

increased the amount of capital gain realized by them on Lawrence's distribution of its assets to them. Lawrence's contract with San Gabriel had a fair market value at the time of its dissolution, equal, at least, to the amount determined by the respondent.

The trade or business of Richard was substantially similar to the trade or business of Lawrence.

Petitioner Albert Gersten and one Theodore Robbins each owned 50 per cent of the outstanding capital stock of a corporation, Homes Beautiful, Inc. Upon the dissolution of such corporation, each stockholder received assets in an amount exceeding $44,721.60. In a proceeding before this Court, Homes Beautiful, Inc., was adjudged liable for deficiencies in its income taxes. The amount of such deficiencies and interest thereon was $44,721.60. Petitioner Albert Gersten paid $40,000 of such sum in December 1947 as a transferee of the corporation's assets and the remaining $4,721.60 on April 5, 1949. Of such payment in 1949, $3,460.47 was applied by the collector to principal and $1,261.13 to interest. Theodore Robbins was insolvent on April 5, 1949.

On the joint return which Albert and Lucille Gersten filed for 1949, they deducted in full the $4,721.60 payment made in that year. The respondent determined that one-half of the total payment, in the amount of $2,360.80, was a payment on behalf of Theodore Robbins and was deductible as a nonbusiness bad debt under the provisions of section 23 (k) (4) of the Code of 1939; that $1,730.23

represented petitioner Albert Gersten's liability as a transferee of the assets of Homes Beautiful, Inc., and was deductible as a long-term capital loss; and that the remaining $630.57 was deductible by him as interest under section 23 (b).

On April 3, 1950, petitioner Lucille Gersten obtained an interlocutory decree of divorce from petitioner Albert Gersten in an action filed in the Superior Court of the State of California in and for the County of Los Angeles. On November 2, 1950, petitioner Albert Gersten obtained a final decree of divorce from Lucille Gersten in the First Civil Court of the State of Chihuahua of the Republic of Mexico, sitting at Juarez. On the same date he married Bernice Anne Gersten in Juarez. The California interlocutory decree was not final on the date of the Mexican divorce and marriage. At all times during the year 1950, petitioner Albert Gersten and Bernice Anne Gersten were residents and domiciliaries of the State of California.

Opinion

Turner, Judge: The first issue raised in the proceedings is whether the payments which the four corporations, Richard, Whittier, Rex and Lawrence, made to San Gabriel were properly included by such corporations in computing the cost of the houses which they constructed and sold. The respondent determined that the amounts paid to San Gabriel were not properly includible by the corporations in computing their cost of goods sold because all such payments were repayable. Petition-

ers, on the other hand, argue that the liability of each of the corporations to pay for the installation of the water facilities was fixed and absolute; and that despite whatever possibility there was of a repayment of part or all of the amounts paid, the payments were none the less properly includible in computing the cost of the houses sold.

In Colony, Inc., 26 T. C. 30, we had much the same question as here.[6] There the corporate taxpayer, which was engaged in the business of subdividing tracts of land and selling lots, made payments to utility companies for the installation of gas and electric service under contracts which called for the repayment of the amounts paid, such repayments to be made by payment of a specified amount for each new customer who purchased service from the gas company's mains or connected to the electric company's lines. The repayments were to be made only for a period of either five or ten years from the date of the contract. The Commissioner took the position that the taxpayer was not entitled to include any part of the payments so made to the utility companies as a part of the cost of the lots which it sold during the taxable years, because of the possibility that all or a part of such payments might be repaid. We concluded that the determining factor was that the taxpayer had made unconditional payments to the utility companies in order to obtain service from them for the purchasers of its

[6] Colony, Inc., was affirmed ... F. 2d ... (April 22, 1957), but there was no appeal on the comparable question herein.

lots. We held that the payments were thus closely related to the sale of the lots and that the taxpayer's income from such sales would be more clearly reflected if a pro rata portion of the payments which it made to the utility companies was included in its basis for determining the gain or loss on each lot sold.

We see no distinguishing difference in that case and the one before us here. It is true that there the repayments were measured by a fixed sum to be paid for each new customer who purchased service from the utility companies, while here the payments depended upon the amount of water sold by San Gabriel in the various subdivisions. But in both cases the controlling facts were that the corporations made unconditional payments to provide utility service for the subdivisions, and such payments were directly related to the property sold. We therefore conclude that the payments which the four corporations here made were a proper item to be included in computing the cost of the property which they sold.

The second issue is whether each of the water contracts which petitioners Albert Gersten, Milton Gersten and Myron P. Beck received from the corporations upon their dissolution had a fair market value at that time. The individual petitioners did not report any value for such contracts in computing the amount of gain realized by them upon the distribution of corporate assets. The respondent determined that each contract had a fair market value, and accordingly increased the amount of

gain reported by the individual petitioners from the distribution of such assets to them.

The petitioners contend that the contracts had no ascertainable fair market value at the time the corporations were dissolved, and citing Burnet v. Logan, 283 U. S. 404; Westover v. Smith, 173 F. 2d 90; and Commissioner v. Carter, 170 F. 2d 911, affirming 9 T. C. 364, argue that the distribution in liquidation did not as to those contracts result in closed transactions and, as a consequence, that no amounts were to be attributed to the contracts at the times of liquidation, but that the payments from San Gabriel subsequent to the dissolutions were to be reported as capital gains as received.

The evidence shows that each of the contracts did have a fair market value at the time the corporations were dissolved, and we have so found. None of the contracts were as much as three years old at the time of distribution, and the payments under them had commenced on all except the Lawrence contract. They began on that one shortly thereafter. All houses had been completed and sold by the time each corporation dissolved. Expert witnesses testified that contracts, similar to those here, were bought and sold, and that one might expect to receive as much as 70 per cent of the total original payment on such similar contracts. There was testimony to the effect that a proposed freeway would cross the subdivision developed by Lawrence. No showing, however, was made that the plans for the freeway route were final, or, if adopted, the extent to which the occupancy of the

houses within the area would be affected during the repayment period. Neither was there any showing that petitioners would or would not have a claim for compensation, if and when their rights to repayment might be destroyed as a result of the building of the freeway.

The record, in our opinion, amply sustains the respondent in his determination of fair market value, and we have so found in our findings of fact.

In Westover v. Smith, supra, and Commissioner v. Carter, supra, the facts were that contractual rights received upon the dissolution of the corporation had no ascertainable fair market value. Here the facts are otherwise. See Pat O'Brien, 25 T. C. 376.

The third issue is as to the deductibility of $4,721.60 paid by Albert Gersten in 1949, in satisfaction of Federal tax liabilities of Homes Beautiful, Inc., a dissolved corporation, of which he had owned 50 per cent of the capital stock and had received 50 per cent of the assets in liquidation. The remainder of the stock had been owned by Theodore Robbins, who likewise had received 50 per cent of the assets of the corporation upon liquidation. The payment of $4,721.60 represented a final payment by Gersten, as transferee, of tax and interest owing by Homes Beautiful, Inc. He had previously paid $40,000 in 1947, and presumably had not been reimbursed by Robbins for any part thereof. It is stipulated that Robbins was insolvent at the time of the final payment in 1949.

On the joint return filed by Albert and Lucille

Gersten for 1949, they deducted the above, $4,721.60 in full. The respondent in his determination treated the payment as having been made by Gersten one-half for his own account and the remainder for the account of Robbins. He further determined that the $2,360.80 treated as having been paid on behalf of Robbins was a nonbusiness bad debt, deductible as a short-term capital loss under section 23 (k) (4) of the Internal Revenue Code of 1939. Of the $2,360.80 treated as having been paid by Gersten on his own behalf, he allowed in full the deduction of $630.57, as representing one-half of the amount which was interest. The remaining $1,730.23 was determined to have been a long-term capital loss under the provisions of section 171 and subject, for deduction purposes, to the limitations of that section.

Taking the position that Robbins had contributed no amount to the tax payments made as transferee of Homes Beautiful, Inc., and relying on Fox v. Commissioner, 190 F. 2d 101, reversing 14 T. C. 1160, and Pollak v. Commissioner, 209 F. 2d 57, reversing 20 T. C. 376, it is the petitioner's contention that as a guarantor he had been called upon to pay the principal obligation of an insolvent debtor, and that the resulting loss, under the cases cited, was a loss incurred in a transaction entered into for profit, within the meaning of section 23 (e) (2), and as such, was deductible in full. On brief, the respondent now takes the position that the entire $4,721.60 is to be regarded as having been paid by Gersten for his own account, that $1,261.13 of

the amount paid was interest, deductible by Gersten in full, and under Arrowsmith v. Commissioner, 344 U. S. 47, the remaining $3,460.47 was a long-term capital loss, which, for purposes of deduction, is subject to the limitations thereon.

That the Fox and Pollak cases do not represent sound law has recently been settled by the Supreme Court in Putman v. Commissioner, 352 U. S. 82, and it follows that petitioner's claim that the loss sustained upon the payment in 1949 was a loss incurred in a transaction entered into for profit under section 23 (e) (2) is not well taken. It also follows, from the pronouncements of the Supreme Court in the Putnam case, that such portion of the payment as was made by Gersten on behalf of Robbins, and for which he had a claim against Robbins, was a nonbusiness bad debt, deductible as a short-term loss under section 23 (k) (4).

As to that portion of the payment which represented a satisfaction of Gersten's own liability as transferee of Homes Beautiful, Inc., Arrowsmith v. Commissioner, supra, is controlling, and the loss sustained was a long-term capital loss.

Whether or not the 1949 payment was in total amount a payment on Robbins' behalf, as petitioner contended in seeking application of section 23 (e) (2), or represented payments on behalf of both Gersten and Robbins in equal amounts, as the respondent determined, presents a question more difficult of solution. We are not advised as to the circumstances relating to the payment of the $40,000 in 1947. The record does not show whether it was

made by Gersten with or without some understanding between him and Robbins. We are only advised that he paid the full $40,000 in 1947, and that at the time of making the final payment in 1949, Robbins was insolvent. The record being as it is, we have found no sound basis for disturbing the respondent's determination herein, under which he treated one-half of the $4,721.60 as having been paid by Gersten for his own account and the other half on account of Robbins. The respondent's determination is accordingly sustained.

The fourth issue is whether petitioner Albert Gersten, and Bernice Anne Gersten, whom he married at Juarez, Mexico, in 1950, were entitled to file a joint income tax return for such year. The respondent has determined that Albert Gersten was not legally married to Bernice Anne Gersten during 1950 and that they therefore were not entitled to file a joint return as husband and wife, as permitted by section 51 (b) of the 1939 Code. [7]

Albert Gersten contends, first of all, that the respondent has neither the function nor the right to challenge the validity of the marriage relationship. We think that argument without merit. Section

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[7] Sec. 51. Individual Returns.
* * * * *

(b) Husband and Wife.—

(1) In General.—A husband and wife may make a single return jointly. Such a return may be made even though one of the spouses has neither gross income nor deductions. If a joint return is made the tax shall be computed on the aggregate income and the liability with respect to the tax shall be joint and several.

51 (b) provides that a husband and wife may make a single return jointly. Obviously, the respondent has not only the right but the duty of determining whether a man and woman who file a joint return are, in fact, legally married and entitled to file such a return under the provisions of the statute. This was made clear in Marriner S. Eccles, 19 T. C. 1049, affd. 208 F. 2d 796; and Commissioner v. Ostler, 237 F. 2d 501, affirming a Memorandum Opinion of this Court filed July 25, 1955.

We said, in Marriner S. Eccles, supra, that marriage, its existence and dissolution, is particularly within the province of the states. Hence, we look to the law of the State of California, the residence and domicile of both Albert Gersten and of Bernice Anne Gersten, to determine if a valid marriage existed between them on December 31, 1950.

Albert Gersten has shown that his second marriage in Mexico was formally solemnized. Under California law, upon such a showing, a second marriage is presumed legal and the former marriage is presumed dissolved. Such presumption, however, is overcome by evidence showing that the former spouse was living and that neither a divorce nor an annulment was ever procured. Goff v. Goff, 52 Cal. App. 2d 23, 125 Pac. 2d 848; Clendenning v. Parker, 69 Cal. App. 685, 231 Pac. 765. No suggestion was made here that Lucille Gersten was not living on the date of Albert's marriage to Bernice, and we know that the California interlocutory decree which she obtained had not become final on that date.

Section 150.1 of the Civil Code of California provides:

§ 150.1 Foreign divorce of parties domiciled in state; effect

A divorce obtained in another jurisdiction shall be of no force or effect in this State, if both parties to the marriages were domiciled in this State at the time the proceeding for the divorce was commenced.

Under California law, actual domicile is necessary to give a court jurisdiction for divorce proceedings, and where there is no domicile there can be no valid divorce. In re McNutt's Estate, 36 Cal. App. 2d 542, 98 Pac. 2d 253. The State of California was a legitimate party involved in any divorce proceedings between Albert and Lucille Gersten, and its courts have sole and exclusive jurisdiction over the marriage status of those domiciled within its boundaries, as all three parties here concerned were. Foreign divorce decrees obtained on assumed residence are not in good faith and are open to attack in the state of true matrimonial domicile. Kegley v. Kegley, 16 Cal. App 2d 216, 60 Pac. 2d 482; Roberts v. Roberts, 81 Cal. App. 2d 871, 185 Pac. 2d 381. The divorce which Albert obtained in Mexico therefore was of no force and effect in California, since it was obtained through assumed residence. In re Davis' Estate, 38 Cal. App. 2d 579, 101 Pac. 2d 761.

The Civil Code of California, Section 61, provides:

§ 61. Bigamous and polygamous marriages; exceptions, absentees

A subsequent marriage contracted by any person during the life of a former husband or wife of such person, with any person other than such former husband or wife, is illegal and void from the beginning, unless:

1. The former marriage has been annulled or dissolved. In no case can a marriage of either of the parties during the life of the other, be valid in this state, if contracted within one year after the entry of an interlocutory decree in a proceeding for divorce. [Emphasis added.]

We think it clear, under the express provisions of the California Code, that Albert and Bernice, who were both residents of the State throughout 1950, were in no position to marry until such time as Albert became finally divorced from his wife, Lucille. The marriage between Albert and Bernice was specifically prohibited by section 61, and void from the beginning. In re Elliott's Estate, 165 Cal. 339, 132 Pac. 439; In re Gregorson's Estate, 160 Cal. 21, 116 Pac. 60; Parmann v. Parmann, 56 Cal. App. 2d 67, 132 Pac. 2d 851; People v. Little, 41 Cal. App. 2d 797, 107 Pac. 2d 634; Vickers v. State Bar of California, 32 Cal. App. 2d 247, 196 Pac. 2d 10.

We therefore conclude that the respondent correctly determined that petitioner Albert Gersten and Bernice Anne Gersten were not legally married on December 31, 1950 and were not entitled

to file a joint Federal income tax return for such year.

The fifth and final issue raised herein is whether the business of J. Richard Company was substantially similar to the trade or business of Lawrence Land Company, within the meaning of section 430 (e) (2) (B) (ii) of the 1939 Code,[8] for purposes of computing its excess profits tax liability for its fiscal period March 1, 1950 to December 31, 1950.

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[8] Section 430. Imposition of Tax.
* * * * *

(e) New Corporations.—
* * * * *

(2) First five taxable years.—For the purpose of this subsection—
* * * * *

(B) The taxpayer shall be considered to have been in existence and to have had taxable years for any period during which it or any corporation described in any clause of this subparagraph was in existence, and the taxpayer shall be considered to have commenced business on the earliest date on which it or any such corporation commenced business:
* * * * *

(ii) Any corporation if a group of not more than four persons who control the taxpayer at any time during the taxable year also controlled such corporation at any time during the period beginning twelve months preceding their acquisition of control of the taxpayer and ending with the close of the taxable year; but only if at any time during such period (and while such persons controlled such corporation) such corporation was engaged in a trade or business substantially similar to the trade or business of the taxpayer during the taxable year. For the purpose of this clause, the term "control" means the ownership of more than 50 per centum of the total combined voting power of all classes

Section 430 imposed an excess profits tax on the income of corporations for each taxable year ending after June 30, 1950, and beginning before January 1, 1954. Subsection (e) of such section imposed a lesser rate of tax in the case of corporations which commenced business after July 1, 1945, and whose fifth taxable year ended after June 30, 1950. The rates of tax so provided were as follows: First and second year, 5 per cent; third year, 8 per cent; fourth year, 11 per cent; fifth year, 14 per cent. For purposes of determining a corporation's years of existence, the subsection provided that, to the actual number of years which a new corporation had been in existence, there was to be added the years prior to its incorporation in which any other corporation had been in existence, if such old corporation was engaged in a trade or business substantially similar to the trade or business of the new corporation, and if such old corporation was controlled by not more than four persons who also

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of stock entitled to vote, or more than 50 per centum of the total value of shares of all classes of stock. A person shall not be considered a member of the group referred to in this clause unless during the period referred to in this clause he owns stock in such corporation at a time when the members of the group control such corporation and he owns stock in the taxpayer at a time when the members of the group control the taxpayer. For the purpose of this clause, the ownership of stock shall be determined in accordance with the provisions of section 503, except that constructive ownership under section 503 (2) (2) shall be determined only with respect to the individual's spouse and minor children.

controlled the new corporation. Lawrence Land Company was incorporated on March 25, 1949, and dissolved on December 31, 1950. In computing its excess profits tax liability under section 430, it claimed that it was a second year corporation within the meaning of the statute. J. Richard Company was incorporated on July 10, 1947, and dissolved on June 22, 1950. Respondent determined that since Albert Gersten and Myron P. Beck owned all of its stock, and since they and Milton Gersten owned all of Lawrence's stock, and since J. Richard Company's business was substantially similar to that of Lawrence, that the years of J. Richard Company's existence prior to the incorporation of Lawrence must be added to those of Lawrence for the purposes of section 430 (e) (2) (B) (ii), and that Lawrence was therefore in its fourth taxable year rather than its second.

We think the respondent's determination was correct. Obviously, both corporations were engaged in the subdividing of tracts of land and in the construction and sale of houses, which we are satisfied was substantially the same "trade or business" within the meaning of the statute. The petitioner attempts to find support for a contrary conclusion in the language of the report of the Senate Committee on Finance, S. Rept. No. 781, 82d Cong., 1st Sess. (1951), p. 73. The report states:

> These special ceiling rates available to new corporations in their period of development are not to be available to new corporations created as the result of either a tax-free reorganization

> or a taxable transaction of the type where, under your committee's action, the purchasing corporation would be entitled to base its income credit on the earnings experience of the predecessor. Your committee believes that such corporations do not truly represent 'new business.' * * *

It further states, however, "They [special ceiling rates] are also denied new corporations which are controlled by persons owning an old corporation engaged in the same business through old corporations." We think the language of the statute itself so clear that no resort need be had to its history in interpreting what it means. But certainly the committee report above referred to does not support a result contrary to the one which we reach here. The businesses of the two corporations were not only similar, but, to our way of thinking, identical. We conclude that the respondent correctly determined that Lawrence Land Company was in its fourth taxable year within the meaning of the statute.

Decisions will be entered under Rule 50.

Served and Entered June 28, 1957.

Tax Court of the United States
Washington

Docket No. 51226

ALBERT GERSTEN, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

DECISION

Pursuant to the Findings of Fact and Opinion of the Court filed June 28, 1957, the parties on October 25, 1957, having filed an agreed computation of the tax involved, it is

Ordered and Decided: That there is a deficiency in income tax for the taxable year 1950 in the amount of $7,847.90.

Entered: Oct. 30, 1957.

[Seal] /s/ BOLON B. TURNER,
Judge.

Served and Entered Oct. 31, 1957.

Tax Court of the United States
Washington

Docket No. 51228

MYRON P. BECK and ANN H. BECK,
Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DECISION

Pursuant to the Findings of Fact and Opinion of the Court filed June 28, 1957, the parties on October 25, 1957, having filed an agreed computation of the tax involved, it is

Ordered and Decided: That there are deficiencies in income tax for the taxable years 1949 and 1950 in the respective amounts of $1,340 and $5,254.68.

Entered: Oct. 30, 1957.

[Seal] /s/ BOLON B. TURNER,
Judge.

Served and Entered Oct. 31, 1957.

Tax Court of the United States
Washington

Docket No. 51229

MILTON GERSTEN and MARY GERSTEN,
Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DECISION

Pursuant to the Findings of Fact and Opinion of the Court filed June 28, 1957, the parties on October 25, 1957, having filed an agreed computation of the tax involved, it is

Ordered and Decided: That there is a deficiency in income tax for the taxable year 1950 in the amount of $1,984.73.

Entered: Oct. 30, 1957.

[Seal] /s/ BOLON B. TURNER,
Judge.

Served and Entered Oct. 31, 1957.

[Title of Tax Court and Docket No. 51226.]

PETITION FOR REVIEW OF DECISION OF TAX COURT

Comes Now petitioner Albert Gersten and petitions for a review of the decision of the Tax Court rendered in the above entitled matter, and alleges as follows:

I.

The above entitled proceeding involves the petitioner's income taxes for the year 1950.

The questions presented are as follows:

(a) Whether certain contracts, assigned and distributed to petitioner upon the dissolution of certain corporations of which he was a stockholder, respectively had or had not ascertainable fair market values on the date of such distribution, for the purpose of determining petitioner's capital gain on the dates of the final liquidations, respectively, of said corporations.

It was the decision of the Tax Court that on the respective dates of said distributions, such contracts did have respective ascertainable fair market values to the extent determined by respondent, and to that extent were required to be included in the computation of petitioner's gain; and

(b) Whether, during the year 1950, petitioner was or was not, under California law, married to Bernice Ann Gersten and accordingly, whether or not petitioner and Bernice Ann Gersten were en-

titled to file a joint return as husband and wife, as permitted by Section 51 (b) of the Internal Revenue Code of 1939.

It was the decision of the Tax Court that in 1950, petitioner and Bernice Ann Gersten were not legally married under California law and therefore were not entitled to file a joint Federal income tax return for such year.

II.

The review is sought before the United States Court of Appeals for the Ninth Circuit.

III.

At all times herein mentioned, petitioner has resided and now resides in the County of Los Angeles, State of California, and filed his income tax return for the year involved with the Collector of Internal Revenue at Los Angeles, California.

The place where the office of said Collector (now Director) of Internal Revenue at Los Angeles is located is within the Circuit of the United States Court of Appeals for the Ninth Circuit, and said Court is the court having jurisdiction of a review of the decision of the Tax Court herein under the provisions of Sec. 7482 (a) of the Internal Revenue Code of 1954, and venue under Sec. 7482 (b) of said Internal Revenue Code.

The decision of the Tax Court was entered October 30, 1957. The time for filing a Petition for Review will therefore expire January 28, 1958, under Sec. 7483 of the Internal Revenue Code of 1954.

Wherefore, your petitioner prays that a review be had of the decision of the Tax Court rendered in the above entitled matter, and that upon such review said decision be reversed.

Respectfully submitted,

/s/ JACOB SHEARER.

Of Counsel:
TANNENBAUM, STEINBERG & SHEARER.

Affidavit of Mailing Attached.

[Endorsed]: T.C.U.S. Filed Jan. 24, 1958.

[Title of Tax Court and Docket No. 51228.]

PETITION FOR REVIEW OF DECISION OF TAX COURT

Come Now petitioners Myron P. Beck and Ann H. Beck, and petition for a review of the decision of the Tax Court rendered in the above entitled matter, and allege as follows:

I.

The above entitled proceeding involves the petitioners' income taxes for the year 1950.

The question presented is whether certain contracts, assigned and distributed to petitioner Myron P. Beck upon the dissolution of certain corporations of which petitioner was a stockholder, respectively had or had not ascertainable fair market values on the date of such distribution, for the

purpose of determining petitioner's capital gain on the dates of the final liquidations, respectively, of said corporations.

It was the decision of the Tax Court that on the respective dates of said distributions, such contracts did have respective ascertainable fair market values to the extent determined by respondent, and to that extent were required to be included in the computation of petitioner's gain.

II.

The review is sought before the United States Court of Appeals for the Ninth Circuit.

III.

At all times herein mentioned, petitioners have resided and now reside in the County of Los Angeles, State of California, and filed their income tax return for the year involved with the Collector of Internal Revenue at Los Angeles, California.

The place where the office of said Collector (now Director) of Internal Revenue at Los Angeles is located is within the Circuit of the United States Court of Appeals for the Ninth Circuit, and said Court is the court having jurisdiction of a review of the decision of the Tax Court herein under the provisions of Sec. 7482 (a) of the Internal Revenue Code of 1954, and venue under Sec. 7482 (b) of said Internal Revenue Code.

The decision of the Tax Court was entered October 30, 1957. The time for filing a Petition for Review will therefore expire January 28, 1958,

under Sec. 7483 of the Internal Revenue Code of 1954.

Wherefore, your petitioners pray that a review be had of the decision of the Tax Court rendered in the above entitled matter, and that upon such review said decision be reversed.

Respectfully submitted,
/s/ JACOB SHEARER.

Of Counsel:
TANNENBAUM, STEINBERG & SHEARER.

Affidavit of Service by Mail Attached.

[Endorsed]: T.C.U.S. Filed Jan. 24, 1958.

[Title of Tax Court and Docket No. 51229.]

PETITION FOR REVIEW OF DECISION OF TAX COURT

Come Now petitioners Milton Gersten and Mary Gersten, and petition for a review of the decision of the Tax Court rendered in the above entitled matter, and allege as follows:

I.

The above entitled proceeding involves the petitioners' income taxes for the year 1950.

The question presented is whether certain contracts, assigned and distributed to petitioner Milton Gersten upon the dissolution of certain corporations of which petitioner was a stockholder, respec-

tively had or had not ascertainable fair market values on the date of such distribution, for the purpose of determining petitioner's capital gain on the dates of the final liquidations, respectively, of said corporations.

It was the decision of the Tax Court that on the respective dates of said distributions, such contracts did have respective ascertainable fair market values to the extent determined by respondent, and to that extent were required to be included in the computation of petitioner's gain.

II.

The review is sought before the United States Court of Appeals for the Ninth Circuit.

III.

At all times herein mentioned, petitioners have resided and now reside in the County of Los Angeles, State of California, and filed their income tax return for the year involved with the Collector of Internal Revenue at Los Angeles, California.

The place where the office of said Collector (now Director) of Internal Revenue at Los Angeles is located is within the Circuit of the United States Court of Appeals for the Ninth Circuit, and said Court is the court having jurisdiction of a review of the decision of the Tax Court herein under the provisions of Sec. 7482 (a) of the Internal Revenue Code of 1954, and venue under Sec. 7482 (b) of said Internal Revenue Code.

The decision of the Tax Court was entered October 30, 1957. The time for filing a Petition for Review will therefore expire January 28, 1958, under Sec. 7483 of the Internal Revenue Code of 1954.

Wherefore, your petitioners pray that a review be had of the decision of the Tax Court rendered in the above entitled matter, and that upon such review said decision be reversed.

Respectfully submitted,

/s/ JACOB SHEARER.

Of Counsel:
TANNENBAUM, STEINBERG & SHEARER.

Affidavit of Service by Mail Attached.

[Endorsed]: T.C.U.S. Filed Jan. 24, 1958.

[Title of Tax Court and Docket Nos. 51226 to 51242, incl.]

STIPULATION OF FACTS

It Is Hereby Stipulated and Agreed, by and between the parties hereto, by their respective counsel, that the facts hereinafter stated shall be taken as true, provided, however, that upon the trial of this case either party hereto shall have the right to (a) introduce other and further evidence not inconsistent with the facts herein stipulated; and (b) object to the materiality of any fact herein stipulated.

J. Richard Co.
Docket—none

1. J. Richard Co. was incorporated July 10, 1947 and dissolved on or about June 22, 1950. The corporation's voting stock was owned during the entire period by Albert Gersten 50% and Myron Beck 50%. The corporation acquired three tracts of land, subdivided them, built homes thereon and then sold the homes.

2. J. Richard Co. contracted for the purchase of 30 acres of land on or about July 17, 1947 and for 10 acres of land on or about August 13, 1947. Escrows covering said parcels were closed and conveyances were made to J. Richard Co. on October 24, 1947 and September 29, 1947. This land became tracts No. 14954 and 15062 referred to in Ex. 1 and consisted of 196 lots upon which 191 homes were built.

3. The Map of Tract No. 14954 was recorded on February 18, 1948, and the first work of any kind performed upon said Tract, consisting of grading, was commenced on or about that date. The first occupancy by a purchaser of a home in said Tract was subsequent to December 15, 1948, and all the homes were sold by June 1, 1949.

4. The Map of Tract No. 15062 was recorded on March 17, 1948, and the first work of any kind performed on said Tract, consisting of grading, was commenced on or about that date. The first occupancy by a purchaser of a home in said Tract was

subsequent to December 15, 1948, and all of the homes were sold by June 1, 1949.

5. J. Richard Co. acquired 5 acres of land on or about February 2, 1948 and 28 acres of land on or about December 22, 1948. The total of 33 acres were contiguous and became the land included in Tract No. 11838 referred to in Ex. 2 and consisted of 163 lots upon which 163 homes were built. The Map of Tract 11838 was recorded on January 19, 1949, and the first work performed upon said Tract, consisting of grading, was commenced on or about that date. The first occupancy by a purchaser of a home in said Tract was subsequent to June 27, 1949 and all of the homes were sold by February 3, 1950.

6. On December 3, 1947 the contract marked Ex. 1 was entered into between Albert Gersten on behalf of J. Richard Co., and San Gabriel Valley Water Co. which concerned the installation of water pipe lines to Tracts No. 14954 and 15062. This contract is referred to on the books of the water company as Job No. 363 W.

6(a). On December 2, 1948 the contract marked Ex. 2 was entered into between Albert Gersten on behalf of J. Richard Co., and San Gabriel Valley Water Co. which concerned the installation of water pipe lines to Tract 11838. This contract is referred to on the books of the water company as Job No. 447 W.

7. A transcript of the 241 ledger of the San Gabriel Valley Water Company for Job No. 363 W is as follows:

Albert Gersten
6363 Wilshire Blvd.
Los Angeles 48, Calif.

Job No. 363 W—Tract No. 15062-14954—Cont. Date 11/21/47—Comp. Date 4/2/48—Expir. Date 11/21/57—Rate: 1/3.

Date	Charges	Credits	Balance
		23,764.00	23,764.00
7-19-48	1.98		23,762.02
10-28-48	55.71		23,706.31
1-24-49	234.55		23,471.76
5-19-49	231.72		23,240.04
9-15-49	384.69		22,855.35
11-16-49	615.04		22,240.31
2-24-50	500.19		21,740.12
6-14-50	301.49		21,438.63
9-26-50	428.97		21,009.66
12-12-50	641.32		20,368.34
3- 1-51	416.37		19,951.97
4-15-51	283.35		19,668.62
8-17-51	453.40		19,215.22
10-17	637.09		18,578.13
1-15-52	433.78		18,144.35
6-24	183.81		17,960.54
9-17-52	493.56		17,466.98
1-19-53	419.53		17,047.45
4-10-53	608.28		16,439.17
7-29-53	188.91		16,250.26
12- 9-53	572.61		15,677.65
12-29-53	502.15		15,175.50
4-14-54	677.42		14,498.08
6-16-54	238.54		14,259.54
July 1954	561.41		13,698.13
Oct. 1954	446.23		13,251.90
Dec. 1954	652.64		12,599.26

8. A transcript of the 241 ledger of the San Gabriel Valley Water Company for Job No. 447 W is as follows:

Albert Gersten
6363 Wilshire Blvd.
Los Angeles 48, Calif.

Job No. 447 W—Tract No. 11838—Cont. Date 12/2/48—Comp. Date 2/28/49—Expir. Date 12/2/58—Rate: 1/3.

Date	Charges	Credits	Balance
		15,258.00	15,258.00
9-15-49	295.05		14,962.95
11-15-49	284.69		14,678.26
2-24-50	396.00		14,282.20
6-13-50	301.89		13,980.31
9-26-50	365.76		13,614.55
12-12-50	375.32		13,239.23
3- 1-51	349.99		12,889.24
4-15-51	263.11		12,626.13
8-17-51	407.27		12,218.86
10-17	554.69		11,664.17
1-15-52	398.98		11,265.19
6-24	244.78		11,020.41
9-17-52	203.18		10,817.23
1-19-53	743.94		10,073.29
4-10-53	302.14		9,771.15
7-29-53	356.21		9,414.94
12- 9-53	250.02		9,164.92
12-29-53	809.80		8,355.12
4-14-54	320.64		8,034.48
6-16-54	427.03		7,607.45
July 1954	242.93		7,364.52
Oct. 1954	775.81		6,588.71
Dec. 1954	305.03		6,283.68

* * * * *

13. All 191 homes in Tracts No. 14954 and 15062, and 11 of 163 homes in Tract No. 11838 were sold by June 30, 1949. The remaining 152 homes in Tract No. 11838 were sold by June 30, 1950.

14. Exclusive of any amounts paid by J. Richard Co. to San Gabriel Valley Water Company during

its year ended June 30, 1948, J. Richard Co. sustained losses in said year of $16,641.04.

15. Upon dissolution and liquidation, J. Richard Co. transferred its assets to its stockholders as follows:

(a) To petitioner Albert Gersten the sum of $38,202.12 in cash, together with a 50% interest in each of the contracts marked Exs. 1 and 2.

(b) To petitioner Myron Beck the sum of $38,-202.12 in cash, together with a 50% interest in each of the contracts marked Exs. 1 and 2.

15(a). J. Richard Company is the same company referred to herein as J. Richard Co.

Whittier Development Co.
Docket 51239

16. Whittier Development Co. was incorporated August 20, 1948 and dissolved on or about December 28, 1950. The corporation was owned during the entire period February 28, 1950 to December 28, 1950, by Albert Gersten 40%, Myron P. Beck 40% and Milton Gersten 20%. The corporation acquired two tracts of land, subdivided them, built homes thereon and then sold the homes.

17. On or about March 25, 1949, Whittier Development Co. contracted for the acquisition for the parcel of land which it acquired on or about August 5, 1949. This land became tract No. 15741, referred to in Exhibit 3, and consisted of 241 lots upon which 238 homes were built. The map of tract 15741

was recorded on August 10, 1949, and the first work of any kind performed upon said tract, consisting of grading, was commenced in May, 1949. The first occupancy by purchaser of a home in said tract was subsequent to June 27, 1949, and all of the homes were sold by June 7, 1950.

18. On or about December 17, 1949, Whittier Development Co. acquired 10 acres of land which became tract No. 14001, referred to in Exhibit 4 and consisting of 53 lots upon which 50 homes were built. The map of tract 14001 was recorded on April 27, 1950, and the first work of any kind performed upon said tract, consisting of grading, was commenced on about that date. The first occupancy by purchaser of a home in said tract was subsequent to November 24, 1950, and all of the homes were sold by December 15, 1950.

19. On or about November 29, 1949, a contract marked Exhibit 3 was entered into between Whittier Development Co. and San Gabriel Valley Water Company which concerned the installation of water pipelines to tract No. 15741. This contract is referred to on the books of the Water Company as job No. 570 W.

20. A transcript of the 241 ledger of the San Gabriel Valley Water Company for job No. 570 W is as follows:

Whittier Development Company
6363 Wilshire Blvd.
Los Angeles 48, Calif.

Job No. 570 W—Tract No. 15741—Cont. Date 11/20/49—Comp. Date — Expir. Date 4/29/59—Rate 35%.

Date	Charges	Credits	Balance
		23,841.00	23,841.00
2-23-50	29.78		23,811.22
6-14-50	503.34		23,307.88
9-26-50	396.22		22,911.66
12-12-50	483.68		22,427.98
3- 1-51	514.23		21,913.75
4-15-51	383.62		21,530.13
8-17-51	548.08		20,982.05
10-17	783.46		20,198.59
1-15-52	555.39		19,643.20
6-24	286.27		19,356.93
9-17-52	480.51		18,876.42
1-19-53	769.34		18,107.08
4-10-53	643.62		17,463.46
7-29-53	376.73		17,086.73
12- 9-53	603.82		16,482.91
12-29-53	865.12		15,617.79
4-14-54	692.92		14,924.87
6-16-54	436.76		14,488.11
July 1954	571.74		13,916.37
Oct. 1954	822.43		13,093.94
Dec. 1954	660.83		12,433.11

* * * * *

25. Whittier Development Company is the same taxpayer referred to herein as Whittier Development Co.

26. Upon its dissolution and liquidation Whittier Development Co. transferred its assets to its stockholders as follows:

(a) To petitioner Albert Gersten the sum of $77,160.26 in cash, together with a 40% interest in each of the contracts marked Exhibits 3 and 4.

(b) To petitioner Myron P. Beck $77,160.27 in cash, together with a 40% interest in each of the contracts marked Exhibits 3 and 4.

(c) To petitioners Milton Gersten and Mary Ger-

sten the sum of $38,580.13 in cash, together with a 20% interest in each of the contracts marked Exhibits 3 and 4.

(d) To petitioners referred to in (a), (b) and (c) a respective 40%, 40%, and 20% interest in a refundable deposit.

Rex Land Co.
Docket 51230

27. Rex Land Co. was incorporated February 4, 1949 and dissolved on or about October 25, 1950. The corporation was owned during the entire period by Albert Gersten 50% and Myron Beck 50%. The corporation acquired one tract of land, subdivided it, built homes thereon and then sold the homes. In addition, a second tract of land was purchased which was subdivided and then distributed to the stockholders upon dissolution.

28. Rex Land Co. acquired land on or about February 15, 1949 which became Tract No. 11960 referred to in Ex. 5 and consisted of 138 lots upon which 138 homes were built. The map of Tract No. 11960 was recorded on March 16, 1949, and the first work performed upon said Tract, consisting of grading, was commenced on or about that date. The first occupancy by a purchaser of a home in said Tract was subsequent to September 12, 1949 and all of the homes were sold by March 16, 1950.

29. On February 9, 1949 a contract, marked Exhibit 5, was entered into between Albert Gersten on behalf of Rex Land Co. and San Gabriel Valley Water Company which concerned the installation

of water pipelines to Tract No. 11960. This contract is referred to on the books of the Water Company as Job No. 429 W.

30. A transcript of the 241 Ledger of San Gabriel Valley Water Company for Job No. 429 W is as follows:

Albert Gersten
6363 Wilshire Boulevard
Los Angeles 48, California

Job No. 429 W—Tract No. 11960—Cont. Date 2/9/49—Comp. Date 4/22/49—Expir. Date 4/22/49—Rate: 35%.

Date	Charges	Credits	Balance
		$14,707.20	$14,707.20
9/16/49	$ 76.59		14,630.61
12/ 6/49	160.24		14,470.37
2/13/50	264.89		14,205.48
6/13/50	281.75		13,923.73
9/25/50	165.55		13,758.18
12/12/50	435.03		13,323.15
3/ 1/51	315.68		13,007.47
4/15/51	213.07		12,794.40
8/17/51	307.32		12,487.08
10/17	442.20		12,044.88
1/15/52	326.43		11,718.45
6/24	207.77		11,510.68
9/17/52	153.07		11,357.61
1/19/53	592.01		10,765.60
4/10/53	249.69		10,515.91
7/29/53	309.49		10,206.42
12/ 9/53	221.21		9,985.21
12/29/53	646.17		9,339.04
4/14/54	241.37		9,097.67
6/16/54	349.43		8,748.24
July '54	195.94		8,552.30
Oct. '54	623.87		7,928.43
Dec. '54	228.42		7,700.01

* * * * *

36. On or about June 22, 1950 Rex Land Co. acquired a parcel of land consisting of approximately 12 acres. This real property became Tract No. 16553 and was recorded on October 3, 1950. Rex Land Co. subdivided this land into 59 lots and installed streets, lights, water and gas. In connection with the final liquidation of Rex Land Co., Tract No. 16553 was distributed equally to Albert Gersten and Myron P. Beck prior to October 25, 1950. Upon final liquidation, this land had a fair market value of $215,350.00.

37. Upon dissolution and liquidation, Rex Land Co. transferred its assets to the stockholders as follows:

(a) To petitioner Albert Gersten $1,158.84 in cash, together with an undivided 50% interest in certain real property having a fair market value of $107,675.00 and a 50% interest in the contract of February 9, 1949, marked Exhibit 5.

(b) To petitioner Myron P. Beck the sum of $1,158.84 in cash, together with an undivided 50% interest in certain real property having a fair market value of $107,675.00 and a 50% interest in the contract marked Exhibit 5.

(c) To each of the petitioners referred to in (a) and (b), a 50% interest in a State tax claim.

37a. Rex Land Company is the same taxpayer referred to herein as Rex Land Co.

Lawrence Land Co.
Docket 51233

38. Lawrence Land Co. was incorporated March 25, 1949 and dissolved on or about December 31, 1950. The corporation was owned during the entire period by Albert Gersten 40%, Myron Beck 50%, and Milton Gersten 10%. The corporation acquired a tract of land, subdivided it, built homes thereon and then sold the homes.

39. Lawrence Land Co. contracted for the purchase of 58.86 acres of land on or about May 18, 1949. This land became tract No. 15650 referred to in Exhibits 6 and 7, which consisted of 287 lots upon which 285 homes were built. The map of tract 15650 was recorded on February 15, 1950 and the first work of any kind performed upon the tract, consisting of grading, was commenced on or about that date. The first occupancy by a purchaser of a home in said tract was subsequent to August 11, 1950 and all of the homes were sold by December 11, 1950.

40. On January 26, 1950 a contract marked Exhibit 6 was entered into between Lawrence Land Co. and San Gabriel Valley Water Company which concerned the installation of water pipelines to tract 15650. This contract was modified by a contract dated February 14, 1950, marked Exhibit 7. These contracts are referred to on the books of the Water Company as job No. 585 W.

41. A transcript of the 241 ledger of the San

Gabriel Valley Water Company for job No. 585 W is as follows:

Lawrence Land Co.
6363 Wilshire Blvd.
Los Angeles 48, Calif.

Job No. 585 W—Tract No. 15650—Cont. Date 2-14-50—Comp. Date 3-29-50—Expir. Date 3-29-60—Rate: 35%.

Date	Charges	Credits	Balance
		31,021.00	31,021.00
3- 1-51	957.08		30,063.92
1-15-52	2,912.56		27,151.36
4-10-53	2,692.46		24,458.90
4-12-54	3,312.43		21,146.47
Dec. 1954	3,274.50		17,871.97

* * * * *

46. Lawrence Land Company is the same taxpayer referred to herein as Lawrence Land Co.

47. Upon its dissolution and liquidation, Lawrence Land Co. transferred its assets to its stockholders as follows:

(a) To petitioner Albert Gersten the sum of $78,382.40 in cash, together with an undivided 40% interest in certain real property having a fair market value of $29,840.00 and a 40% interest in the contracts marked Exhibits 6 and 7.

(b) To petitioner Myron P. Beck the sum of $97,978.00 in cash, together with an undivided 50% interest in certain real property having a fair market value of $37,300.00 and a 50% interest in the contracts marked Exhibits 6 and 7.

(c) To petitioners Milton and Mary Gersten the sum of $19,595.59 in cash, together with an undivided 10% interest in certain real property having

a fair market value of $7,460.00 and a 10% interest in the contracts marked Exhibits 6 and 7.

* * * * *

Albert Gersten—1950
Docket 51226

53. On April 3, 1950, Petitioner Lucille Gersten obtained an interlocutory decree of divorce from Petitioner Albert Gersten in an action filed in the Superior Court of the State of California in and for the County of Los Angeles, entitled Lucille Gersten vs. Albert Gersten, Case No. D-382,738.

54. On November 2, 1950, Petitioner Albert Gersten appeared before the judge of the First Civil Court of the State of Chihuahua of the Republic of Mexico at Juarez, and obtained a final decree of divorce from said Lucille Gersten. Subsequent thereto, but on the same day in Juarez, Petitioner Albert Gersten married Bernice Anne Gersten.

55. The California interlocutory decree, Case No. D-382,738, was not final at the time of the Mexican divorce and marriage on November 2, 1950.

56. At all times during the year 1950, Petitioner Albert Gersten and Bernice Anne Gersten were residents of the State of California.

57. Petitioner reported his one-half interest in land received by him from the liquidation of Rex Land Co. (referred to herein at Paras. 36 and 37) at a fair market value of $118,000.00. The notice of deficiency and petition do not disturb this valuation. However, the valuation is hereby raised as an issue in this proceeding and the fair market value is agreed to be $107,675.00.

58. In Docket 51226 petitioner concedes all issues in the notice of deficiency except as follows:

(a) Respondent's determination that Albert Gersten is not entitled to file a joint return with Bernice Anne Gersten for 1950;

(b) An adjustment of $11,104.87 referred to as Item (a) Long-term capital gain on page 2 of the notice of deficiency attached to the petition; and

(c) The valuation of certain land referred to in Para. 57 hereof.

Myron P. Beck and Ann H. Beck—1949-1950
Docket 51228

59. Petitioners reported their one-half interest in land received by them from the liquidation of Rex Land Co. (referred to herein at Para. 36 and 37) at a fair market value of $118,000.00. The notice of deficiency and petition do not disturb this valuation. However, the valuation is hereby raised as an issue in this proceeding and the fair market value is agreed to be $107,675.00.

60. In Docket 51228 the petitioners concede all issues except as follows:

(a) The adjustment of $12,982.93 referred to as Item (a) long-term capital gain on page 3 of the deficiency notice attached to the petition.

(b) The valuation of certain land referred to in Para. 59 hereof.

Milton Gersten and Mary Gersten—1950
Docket 51229

61. In Docket 51229 petitioners concede all issues except an adjustment of $2,238.55 referred to as Item (a) long-term capital gain on page 1 of the notice of deficiency attached to the petition.

Transferees

62. The following parties are liable as transferees of the assets of the following corporations in the amount of the corporate deficiencies determined in this proceeding:

Transferor		Transferee	
Name	Docket No.	Name	Docket No.
J. Richard Co.	None	Albert Gersten	51237
		Myron P. Beck	51238
Whittier Development Co.	51239	Albert Gersten	51240
		Myron P. Beck	51241
		Milton Gersten	51242
		Mary Gersten	51242
Rex Land Co.	51230	Albert Gersten	51231
		Myron P. Beck	51232
Lawrence Land Co.	51233	Albert Gersten	51234
		Myron P. Beck	51235
		Milton Gersten	51236
		Mary Gersten	51236

In Dockets 51232, 51235, 51238 and 51241. Ann H. Beck is not the transferee of any of the corporations referred to in those dockets.

General

63. At all times material hereto, San Gabriel Valley Water Company (hereinafter sometimes referred to as "San Gabriel") was a California water utility corporation subject to the regulatory juris-

diction of the Public Utilities Commission of the State of California.

64. None of the purchasers of any of the residences included in any of the tracts above mentioned were required, by or in connection with the contract of purchase of the residence, to use or purchase water from San Gabriel, in any amount, or for any period, or at all.

65. San Gabriel Valley Water Company holds a franchise for the area in which Tracts 14954, 15062, 11838, 15741, 14001, 11960 and 15650 are located.

66. Tracts 14954, 15062, 11838, 15741, 14001, 11960, 15650 are located in the same neighboring area.

67. There were substantially no vacant houses in the neighboring area referred to in Para. 66 hereof during 1948, 1949 and 1950.

68. The respective tracts subdivided and developed by each of J. Richard Co., Whittier, Lawrence and Rex were not contiguous to the tracts of any of the other of said corporations.

69. The water contracts marked Exs. 1, 2, 3, 4, 5, 6 and 7 were transferable at the request of the party who owned the contracts with San Gabriel Valley Water Company.

70. Exs. 1 through 7 and A through O are attached to this stipulation and made a part hereof.

71. All refunds made under the contracts shown on Exs. 1, 2, 3, 4, 5, 6 and 7 received before disso-

lution of the corporations were credited and offset against the cost of houses sold on the corporate books except $235.55 and $231.72 received on January 24, 1949 and May 19, 1949, respectively, by J. Richard Co.

72. The extension of the pipe lines for the service of water provided for in Exs. 1, 2, 3, 4, 5, 6 and 7 was essential to the subdivision and sale of the subdivision tracts herein involved and in the absence of the refund provisions of said Exs. 1, 2, 3, 4, 5, 6 and 7 would have been properly added to the cost of the houses sold with respect to each of the subdivision tracts.

73. Each of petitioners, Albert Gersten, Lucille Gersten, Myron P. Beck, Milton Gersten and Mary Gersten, kept books and reported their income upon a cash basis of receipts and disbursements.

* * * * *

75. The minimum rate per month for water consumers which was charged by San Gabriel Valley Water Company during the periods 1948, 1949 and 1950 was $1.25.

76. None of the petitioners herein held title to the water pipe line installations which are referred to in Exs. 1, 2, 3, 4, 5, 6 and 7.

77. The payments to San Gabriel Valley Water Company referred to in Exs. 1, 2, 3, 4, 5, 6 and 7 were paid on or about the date of the contracts.

78. The words "cont." and "comp." used in the 241 ledger of San Gabriel Valley Water Company mean contract and completion respectively.

79. None of the refunds from the contracts marked Exs. 1, 2, 3, 4, 5, 6 and 7 were reported by the former stockholders after the corporations were dissolved until some time in either December, 1952, or January, 1953, at which time amended returns for the year 1951 were filed in which all refunds to December 31, 1951 were reported.

/s/ JACOB SHEARER,
Counsel for Petitioners.

/s/ R. P. HERTZOG,
Acting Chief Counsel, Internal Revenue Service, Counsel for Respondent.

[Endorsed]: T.C.U.S. Filed April 29, 1955.

[Title of Tax Court and Docket Nos. 51226 to 51242, incl.]

SUPPLEMENTAL STIPULATION OF FACTS

It Is Hereby Stipulated and Agreed, by and between the parties hereto, by their respective counsel, that on July 1, 1950 the San Gabriel Valley Water Company had outstanding 277 water facilities contracts.

/s/ JACOB SHEARER,
Counsel for Petitioners.

/s/ JOHN POTTS BARNES,
Chief Counsel, Internal Revenue Service, Counsel for Respondent.

[Endorsed]: T.C.U.S. Filed Aug. 24, 1955.

In the Tax Court of the United States

Docket Nos. 51226 to 51242, incl.

ALBERT GERSTEN, et al., Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

TRANSCRIPT OF PROCEEDINGS

U. S. Post Office, Courtroom No. 9, Los Angeles, California, Friday, April 29, 1955.

The above-entitled matter came on for hearing, pursuant to notice to the parties, at 10:15 o'clock a.m.

Before: Honorable Bolon B. Turner, J., Presiding.

Appearances: Jacob Shearer, Esq., 6535 Wilshire Boulevard, Los Angeles, California for the petitioners. George E. Constable, Esq., (Hon. Daniel A. Taylor, Chief Counsel, Internal Revenue Service) for the respondent. [1]*

Proceedings

The Clerk: Docket 51226, et cetera, Albert Gersten and associated cases.

Will you state your appearances, gentlemen?

Mr. Shearer: Jacob Shearer for all petitioners.

Mr. Constable: George E. Constable for respondent.

* Page numbers appearing at top of page of Reporter's Transcript of Record.

The Court: All right, Mr. Shearer, you may state the case.

Mr. Shearer: There are several issues in this case, your Honor, to dispose of; some minor ones I will dispose of, one relating solely to the petitioner Albert Gersten. That issue is the right to deduct a portion of the transferee liability in another case for which he was liable to the Government, which was paid by him by reason of the insolvency of his equal co-stockholder, both at the time of the determination of that deficiency and the time of payment of it.

The issue also involves his right to deduct all of the interest in connection with that payment, rather than one-half.

The Court: What do you mean "rather than one-half"?

Mr. Shearer: Respondent has disallowed one-half the interest on the theory that the payment was made apparently on behalf of the insolvent other stockholder and treats it along with half of the principal paid as a non-business bad debt. [3]

Our position is that as to the entire principal, the payment was made in the nature of a guarantor, and that petitioner is entitled to deduct it as a loss incurred, and that in any event, as to the interest, that he is liable for the entire amount and is entitled to deduct.

The Court: Why do you say that?

Mr. Shearer: Why do I say he is entitled——

The Court: To deduct it all?

Mr. Shearer: Because the stipulation will show

that he was fully liable to the Government for all of the interest. He paid the interest which he was obligated to pay.

The Court: He has a right of collection against any other party that is liable, doesn't he?

Mr. Shearer: Yes, your Honor, he has such a right of collection, providing he can collect it. But the interest which he pays is——

The Court: It wasn't his interest, was it?

Mr. Shearer: The Government didn't think so when they demanded it.

The Court: All right. Go ahead.

Mr. Shearer: The second issue relates again solely to the petitioner Albert Gersten, and it relates to the validity of a Mexican divorce and subsequent remarriage in relation to petitioner's right to file a joint return with his wife, that is, the lady whom he married after the Mexican divorce. [4]

The Court: I didn't get that exactly.

Mr. Shearer: The petitioner Albert Gersten obtained a Mexican divorce. Subsequent to that divorce, in the year 1950 he married, and the issue here presented is whether he may file a joint return for the year 1950 with the lady whom he married subsequent to the Mexican divorce. Both the divorce and the marriage took place in Mexico.

In that connection petitioner's former wife had obtained an interlocutory decree in 1950 in California. That decree was not final at the time of the Mexican decree. Respondent contests the validity of the Mexican divorce and, as a result, contests peti-

tioner's right to file the joint return with the second wife.

It is our position, first, that the Mexican decree was valid for this purpose and, second——

The Court: Why do you say, "for this purpose"? If it is valid, it is valid, isn't it?

Mr. Shearer: I don't think that is necessarily the law, your Honor. I think that there are void and voidable marriages, void and voidable divorces. A marriage, even though voidable, may be voidable only at the petition or instance of specific persons. We insist that even if this marriage is or was voidable, we don't concede that—the Commissioner of Internal Revenue is not one of those persons who may assert its invalidity. [5]

The Court: I would be interested in your brief on that.

Mr. Shearer: Yes, your Honor. There are, we think, both cases and rulings of the respondent itself in connection with that matter, which we will submit on brief.

The issue common to all of the corporate cases stems from separate transactions which each of these corporations entered into with the San Gabriel Valley Water Company. Each of the corporate taxpayers was engaged in the business of subdividing raw land, building homes thereon, and selling those homes. In order to comply with the requirements of California law relating to subdivisions, and in order to make water available to the homes, each of the corporations entered into separate contracts with San Gabriel, which was a privately

owned water company but subject to regulatory jurisdiction of the Public Utilities Commission of the State of California.

Each contract called for a given payment by the subdivider to San Gabriel, and that payment was determined by the cost of the water pipe installation which San Gabriel was to make and did make. The payment was in consideration of San Gabriel's agreement to extend its pipe lines and to make these installations for the service of water to the tract covered by the contract.

The pipe lines were laid in publicly dedicated streets and were not owned by the corporate taxpayers. Each of [6] the contracts also provided—and this provision was a requirement under the rules of the California Public Utilities Commission —that refunds or repayments were to be made by San Gabriel to the subdivider in question upon a contingent basis, that contingency being to the extent of a given percentage of revenues derived by San Gabriel from the sale of water to occupants of the particular subdivision and derived within the limited period of time, that is to say, ten years.

This ten-year period commenced in some of these cases when the contract was made, before any work in the way of water installations had commenced; and in other of the cases when the water pipe lines work had been completed, not the subdivision work, but the water pipe line installation had been completed.

The Court: When you say "revenues" you mean water sales?

Mr. Shearer: Sales, made by San Gabriel to occupants of the proposed homes. It is important in this connection to bear in mind that either the contract date, the contract with San Gabriel or the completion date—San Gabriel's completion date—were in all cases dates which considerably preceded the completion of any of the homes in the given subdivision and considerably preceded the sales and occupancies of those homes. The time lag, however, varied in several cases.

The Court: If they sold that much water, it wouldn't [7] make that much difference, would it?

Mr. Shearer: They sold how much water?

The Court: After the homes were completed, if the water company sold enough water to take care of the amount, it wouldn't make any difference whether the homes were completed or whether they weren't at the time of the period, would it?

Mr. Shearer: No water sales were made until after the occupants' homes were completed.

The Court: Well, that would be a rather obvious fact, I would assume, unless there was some temporary pipe in there for the use of water in construction.

Mr. Shearer: There were some, but those were completely trivial.

The Court: My query wasn't directed to that at all.

Mr. Shearer: I don't follow your Honor's query.

The Court: You say there was a ten-year period, but none of the homes were completed at the time

the ten-year period started to run, as I understand you.

Mr. Shearer: That is right.

The Court: All right. Suppose six years has elapsed before any home was completed and before any water was delivered by San Gabriel to occupants of homes, but in the remaining four years they used enough water to—the required amount of water. It wouldn't make any difference, would it, whether it was done in four—— [8]

Mr. Shearer: What we are concerned with is what do we do with the payment made by San Gabriel in the year involved.

The Court: In what way does it make a difference?

Mr. Shearer: It makes this difference——

The Court: If they pay out and get the refund?

Mr. Shearer: It makes a difference. And it wasn't a matter of six years. At that stage of the game, the subdivider doesn't know whether he is going to get his refund or not, or how much, or what rate.

The Court: I am assuming a situation where he does.

Mr. Shearer: Then you have a problem of whether they can sell enough water in four years to make these refunds.

The Court: My proposition was that they did sell enough water. I wasn't assuming a case where they didn't or there wasn't enough sold.

Mr. Shearer: My contention is that that is hind-

sight, with which we are not concerned for this purpose.

The Court: All right. Why?

Mr. Shearer: It is taxpayer's position that these payments constituted a portion of the cost of the property sold by it, that is, that the payments——

The Court: I understand that.

Mr. Shearer: In order to properly reflect its [9] income, it was entitled to, and we think under the law required to, add in the year in which the payment was made or accrued those payments to the cost of the property which it sold, notwithstanding the possibility of recoupment; failure to recognize this result might involve the taxation of return of capital rather than of income, and the language I have just used—and our position—is substantially the position and language of the Security *Flower* Mills case and the Freehaufer Baking Company case.

It is our position basically that the contingency that may arise later with respect to recoupment is not a contingency to be considered in determining the net income of taxpayer in the year of payment.

The Court: Well, I doubt that you will find the same situation here as was present in the Security Flower Mills.

Mr. Shearer: I used the word "language", your Honor, the language of the Security Flower Mill. I do think we have the identical situation with the Freehaufer case.

The Court: You have to read language along

with the facts with respect to which the language is used.

Mr. Shearer: I understand that, your Honor. The concept there involved was adopted in substantially similar circumstances in the Freehaufer case.

The language to which I referred was quoted with approval, and I think we have there the cases substantially on [10] all 4's with our case in principle, and very close to it, in fact, except that in one case you are dealing with bread and flower and the other with land and water.

I am stating our position, your Honor.

The Court: I understand you were stating your position, but I was trying to get an understanding of your position by proposing a set of facts, but you apparently don't want to discuss them, so go ahead and possibly we will get at it on brief.

Mr. Shearer: I think this may come in when I follow on with respondent's position in this matter, because respondent has determined that these payments to San Gabriel by the subdividers are capital expenditures. But they are not, he says, capital expenditures for the water pipe lines, which the subdividers don't own, but capital expenditures for the right to receive back, perhaps, the capital expenditures. In other words, it is respondent's position that the payments made are for a contract to receive under limited conditions, in the light of certain contingencies, to receive back the very payments made; for that reason it is an acquisition of property rather than a part of the costs of goods sold in connection with the subdivided land.

Our position is that such a determination is completely unrealistic in this sense, that if there is one thing sure in connection with this, the subdivider can never receive [11] more than that which he pays, and to treat this as an investment or purchase transaction by the subdivider is entirely unreal and escapes the real meaning of the transaction.

The Court: Do you take the position that the corporations gave up all right and interest in this money so paid in, is that right?

Mr. Shearer: Yes, without a question they did.

The Court: All right.

Mr. Shearer: I think that is stipulated to.

The Court: Go ahead.

Mr. Shearer: I don't mean to infer——

The Court: I am not talking about earmarked dollars, mind you.

Mr. Shearer: Yes, I understand. What I am saying is that the payment was absolute and without right to repayment excepting as certain contingencies might occur. When I speak of stipulation, I am referring to that limited phase of it. I don't mean that respondent has stipulated that there were no rights of refund.

Your Honor mentioned the six-year period, and actually the period here involved, the lag period, will not reach anything like six years.

The Court: Apparently you weren't paying attention to what I was saying. I was supposing a case where it did. I wasn't saying that these did. I rather imagined they didn't. [12]

Mr. Shearer: Yes, I understand. However, I

took it that your Honor's example was to pose an extreme example.

The Court: I was giving you an exaggerated case to try to get you to give me some light on that situation, and maybe I could better understand your contention. But we will pass that now. Let's go ahead.

Mr. Shearer: Now, the common issue in the individual cases relates to the treatment, for the purpose of determining capital gain on the dissolution of these corporations, the treatment of the rights to receive refunds under these same contracts. We take the position that although, by the time of dissolution——

The Court: What individuals are you talking about and how did they obtain any right?

Mr. Shearer: All of the individual petitioners here, with the exception of Lucille, who was not concerned with this, were stockholders of various corporations in varying amounts.

The Court: These were the corporations that were building the houses?

Mr. Shearer: That is right.

The Court: And having the water lines run?

Mr. Shearer: These were the corporate petitioners here involved.

The Court: I bring that out, because now, mind you, [13] while we did go into this a bit at the call of the calendar, I am trying to get a clear statement of the issues here for the opening of this trial so we will have it in this transcript. So don't assume, be-

cause we covered something in the discussion here at the call of the calendar, that it will appear here in this transcript.

Mr. Shearer: Yes, your Honor.

The common issue with respect to the individual petitioners is their position as stockholders who received these rights under the water contracts to which we are now referring, upon the dissolution of the corporations. I won't here try to segregate which individuals received from which corporation.

The Court: About how long after the deposits or the paying of this money for the running of the water mains did the dissolutions occur?

Mr. Shearer: The time varied between approximately one to two years. But in each case, by that time, all of the homes had been built and all of the homes had been sold and substantially all of them, if not all of them, were by that time occupied.

Now, we take the position that in spite of the fact that some of the contingencies with which the subdivider was faced at the time he made the payments no longer existed at the time of the dissolution, contingencies such as delays in [14] completion for various reasons—and at the time of dissolution, substantially complete occupancy had been established — nevertheless, even at that time there remained sufficient other contingent factors with respect to the rights to receive these payments from San Gabriel which were beyond the control of both the taxpayers and, for that matter, of San Gabriel, which precludes the ascertainment of a fair market value at the time of dissolution of these rights

under the doctrine of Burnett versus Logan and Westover versus Smith.

The Court: Were these subdivisions located in the same general area?

Mr. Shearer: In the same general area.

The Court: Where?

Mr. Shearer: In Los Angeles County near the city of Whittier.

The Court: All right.

Mr. Shearer: That is not to say that the subdivisions all represented the same quality of property, a fact that comes into another issue. What I am trying to say is that there are better and worse locations in and around the city of Whittier, so that property is more or less valuable by reason of that.

The Court: That is usually the case around most cities, I have noticed.

Mr. Shearer: Yes, your Honor, and this area is no [15] exception. That is my point. I didn't wish the phrase, "the same general area," to blanket in that exception.

Now, respondent contends that the rights under the water contracts had, at the time of dissolution, a fair market value of 50 percent of the then unpaid balance thereof, there having been some payments made prior to the dissolution. On this issue we are relying solely on the Burnett versus Logan doctrine.

The Court: Wherein is that comparable?

Mr. Shearer: In the Burnett-Logan the sale was made——

The Court: Sale of what?

Mr. Shearer: Sale of a contract — the sale of stock was made with a sales price—purchase price was measured there by the amount of coal ore which was mined——

The Court: What sort of ore?

Mr. Shearer: Coal.

The Court: Coal?

Mr. Shearer: Coal.

The Court: Are you sure?

Mr. Shearer: Yes, your Honor. The contract stipulated that for each ton of coal mined by the corporation, whose stock was sold, the seller of that stock was to receive a given amount.

The Court: From whom were they to receive it?

Mr. Shearer: They were to receive it from the purchaser of the stock, not by the corporation whose stock was sold. The court made clear there that there was no obligation on the part of the operating company to mine one or more tons of ore during the life of this contract, although the opinion also makes it clear that at the very time of the sale coal was in fact being mined and that the contract unquestionably had a substantial value, the case going off on the proposition of not an ascertainable value, and the lack of need in the circumstances for income tax purposes to make that determination. That is our position here, except that here we have dissolution instead of the sale. At the moment of dissolution the purchasers, as it were, that is, the distributing stockholders, are entitled to receive payments dependent upon the use by third persons of the water. At that time there was no obligation

on the part of the purchasers of the water users to use that water although, just as in Burnett versus Logan — and for that matter in Westover versus Smith—under similar circumstances——

The Court: What are the circumstances in Westover versus Smith?

Mr. Shearer: That was a dissolution case. The corporation had sold patents; part of the sales price involved was the right to receive specific amounts measured by the patent products manufactured by the purchaser. There was no [17] requirement by the purchaser to manufacture any given amount at any given time.

The Court: When was that decided, in what court?

Mr. Shearer: That was decided in 1949 and was decided in the 9th Circuit. In that case the Court expressly stated, as a matter of fact, that the contract without question had a very substantial value, and the facts so indicated, because in fact the purchaser of the patent was producing the patented product and at the very time of dissolution was busy paying to—had paid to the corporation prior to the time of dissolution and continued to pay and was in the business of producing and continued to pay. The question there was how you measure this, just as we submit here; the question is not that people won't use water, but how do you measure what the stockholders are going to receive, because there is no reasonable way of measuring it.

Our position is that the tax collector waits and collects as the stockholders receive these refunds.

That was the position of the Supreme Court in Burnett versus Logan. It was the position of the 9th Circuit in Westover versus Smith, and it is our position here.

Now, in the case of the petitioner Lawrence Land Company, we have an issue as to excess profits taxes, whether the excess profits taxes should under Section 430 (E)(1) be computed at the rate for second-year corporations or fourth-year [18] corporations. Your Honor may recall that the second taxable year is smaller than the fourth taxable year rate, and of course petitioner is contending for the second and respondent for the fourth. This issue will turn upon the meaning intended by Congress to be given to the phrase "engaged in a trade or business substantially similar to the trade or business of the taxpayer," and relating to a prior corporation. This is an attribution section.

The Court: I don't follow you on your situation that you are talking about.

Mr. Shearer: I am about to come to it. This is a section which accepts the right of new corporations in given cases to use what is in fact their second year if stockholders of that corporation have owned or acquired within the period specified by the statute, stock of another corporation which was engaged in a similar trade or business to the trade or business of the taxpayer and which had an earlier taxable year.

The Court: Apply it to this case.

Mr. Shearer: I was about to. In this case there is no quarrel here at all about the facts in the sense

that the control in this case—the stockholders of Lawrence Land Company did, in fact, acquire within the prescribed period of time, stock and had the control of the stock of J. Richard Company, an earlier corporation.

Respondent's position is that the rate for Lawrence [19] must be computed for the fourth year because had J. Richard continued it would have been in the fourth year, in its fourth year of business. We concede that if Congress intended that the word "similar" related to industry similarity, our position is that what Congress, having in mind the purpose of the legislation which was to avoid splitting of corporations and having the new corporations pick up at a lower excess profits tax rate than those already in existence, what Congress was intending to do there was to limit its special rate for new corporations to corporations which truly started a new business. For that reason, even though concededly J. Richard and Lawrence, the two corporations here involved, were both in the business of subdividing land, there was the industry similarity, we will argue that the meaning of this particular phrase was related to a different kind of similarity, a similarity as to specific businesses. There will be little fact produced at the trial in connection with this beyond the stipulated facts, since most of the underlying facts are stipulated.

The Court: Well, I think I will have to read your brief to understand what you are talking about exactly there.

Mr. Shearer: I think, your Honor, this is the kind of issue which is better left to the brief, and I don't think further clarification will aid in the trial because, as I say, there will be very little in the way of evidence relating to this issue that isn't already in the stipulation. [20]

That about states it. There are transferee cases, but those issues have been stipulated. I do want to address myself to the stipulation when that is offered, but I will wait until then.

The Court: All right.

Mr. Constable: Your Honor, I have several points I would like to clear up before I offer any discussion on the perhaps main points involved.

We have entered into a very lengthy stipulation of facts, and it was only just last night that we completed it, so I would like at this time to clean up some tag ends on it if we may.

The Court: I would rather that you go ahead and state your issues before you start into matters pertaining to the stipulation of facts. I would like to have you state the points of difference on the statement of petitioners' counsel and any points of agreement; and on the points of difference, what the basis for them is.

Mr. Constable: In the first instance, referring to all the transferee dockets, in paragraph 62 of the stipulation petitioner has agreed that the petitioners in the transferee cases are transferees if there is a deficiency determined to the corporations, with the exception of one petitioner, they have so agreed,

and respondent has agreed that that particular petitioner is not a transferee. [21]

Now, referring to the corporation cases, there are four corporations. We call them Rex, Richard, Whittier, and Lawrence. Richard is not a docketed case but it is involved because of the valuation problems, valuation of its assets as transferred to the stockholders, so that Richard is in issue here through the stockholders' case. In all of the corporate cases, the water contract, as petitioner claims deductibility of the deposits made, is in issue. I think petitioner contends that these deposits are either costs of goods sold or in the alternative they are an expense.

The Court: How is that?

Mr. Constable: I think that petitioner, if I am correct, alternatively claims that the deductions in the case of water contracts to the corporations are, in the first instance, deductions in cost of goods sold.

The Court: That is my understanding.

Mr. Constable: Yes.

The Court: That is part of the cost of these houses that they sold.

Mr. Constable: That is correct. And respondent feels that the issue is more properly framed within that scope, but as I understand it now, petitioner feels that as an alternative these matters are deductible as expense.

The Court: I hadn't so understood.

Mr. Shearer: No. To explain that, we had so

[22] pleaded originally, assigned error to that, but our position is, cost of goods sold.

Mr. Constable: In Whittier Development Company, 51239, there are two years involved, but the latter year involves an overassessment and so is not in issue.

The Court: The petitioners' point is that this is part of the cost basis, these payments to the water company. What is the respondent's position?

Mr. Constable: I am coming to the meat of the deductibility of the water deposits now.

The Court: All right.

Mr. Constable: I think petitioner relies improperly on Burnett versus Logan. For one thing, in that case I believe it is iron and not coal, if I am not mistaken.

The Court: I think that is right.

Mr. Constable: In that case.

The Court: My memory I don't think would play me false on it, although that case was decided many, many years ago and I haven't looked at it in years, but I rather think it is iron ore.

Mr. Constable: Involved the Mahoney Mine, I think.

The Court: At least that is my recollection; I could be wrong.

Mr. Shearer: I will stipulate it was either coal or iron. [23]

The Court: It doesn't make any difference, I don't think. It might.

Mr. Constable: No, I don't think so.

The Court: It might. There might be some dif-

ference between mining coal and mining iron ore, I don't know. But go ahead.

Mr. Constable: In Burnett versus Logan we of course had the question from the other standpoint. We had a question of whether or not certain payments to be received in the future were income or not, and the case is perhaps distinguishable on that point.

The Court: What is that?

Mr. Constable: The case is perhaps distinguishable in that in the Burnett versus Logan case we had the question of whether or not certain payments to be made in the future, which were not ascertainable, whether or not the market value of those payments at a given date was to be taken into income. I believe that is the issue in Burnett versus Logan.

In our case we have the reverse situation. We have the question of whether or not an expenditure made for which recoupment is probably coming, whether that expenditure is an allowable deduction.

The Court: Or part of the cost basis?

Mr. Constable: That is correct, your Honor.

The Court: And the petitioner says they are [24] relying on the cost basis proposition, not a deduction.

Mr. Constable: All right.

The Court: Just what is the Government's view of it?

Mr. Constable: Well, your Honor, in Burnett versus Logan, I think the Government also relies on that case as standing for one of the basic concepts

of realization. In that case the Court looked, I believe, to the matter of probabilities and simply said, "We can wait and see in the case of this taxpayer just exactly what is realized from this transaction," and that is essentially the Government's case here, that the expenditure is made by the builder, and rather than allow him a deduction as his cost in the year that it is made, relying on the Logan case, we feel that we can wait until the ten-year period is expired and at that time determine with absolute accuracy the realization of the loss or the realization of what is a deduction at that time.

The Court: Well, whatever the Supreme Court had in mind in Burnett versus Logan, the effect was to put it on a cash receipts basis, those sellers of stock.

Mr. Constable: That is correct, your Honor.

The Court: All right.

Mr. Constable: In Burnett versus Logan the Court is, I think, establishing the concept of realization, gains and losses, and felt that to invoke principles of guesswork as to what iron would come out of this mine in the future was [25] something that, rather than to guess, we can just wait and see.

The Court: The so-called valuation experts would resent that statement of yours that that is guesswork.

Mr. Constable: Now, interestingly enough, there is a case—what is a very popular case—the Cohan case which, in addition to its popular point, has in it a problem very similar to our situation here. Cohan and Harris were co-owners of a lease on the

Chicago Opera House in Chicago, and they put their own plays on in this opera house under the lease that they jointly held, each having a 50 percent interest. Time went on; differences arose, and it seemed that each wanted priority on his particular plays, so they made an agreement whereby Cohan would loan Harris $150,000 and Harris would repay the $150,000 to Cohan from his share of the receipts from the theater. Now, the reason this loan was made as part of their agreement, Harris would then give up all rights to having his plays shown in the theater. In other words, Cohan wanted the theater exclusively, so he loaned $150,000 to Harris so that Harris could go out and finance his plays in other buildings.

Now, there was no personal obligation on the part of Harris to repay the $150,000.

The Court: Except out of profits.

Mr. Constable: Except out of the profits of the theater. Now, without getting into the details of the specific issues involved in that case, I think it holds that the [26] $150,000 was not deductible by Cohan in the year that it was made, and there we have a very similar situation. We have the repayment, dependent entirely upon the profits of the theater.

The Court: Where and when was that case decided?

Mr. Constable: That was the Second Circuit in 1930, your Honor, Learned Hand's opinion.

The Court: That is not The Cohan case?

Mr. Constable: That is The Cohan case.

The Court: That was one of the issues in it?

Mr. Constable: That is correct, your Honor.

The Court: Well, it has been completely lost by the use of the other one, I must say.

Mr. Constable: Now, another thing that I think is fundamentally wrong with petitioners' position with regard to the inclusion of these deposits into its cost of goods sold is that they are confusing what is a contingent liability with what is an absolute liability but payments to be ascertained. I don't want to say payments contingent, but perhaps that is it, that here we have an absolute—we have not a contingent liability. We have a fixed, determined liability, but the payments are uncertain.

The Court: What is the difference?

Mr. Constable: Well, I think this, your Honor. I don't want to rely on what our brother accounts to in connection with matters like this, but there they go to great [27] lengths in distinguishing between a situation where a man has an actual liability that exists as such but they don't know how much it is; in that case they don't call that a contingent liability. They call it an existing liability and set up a reservation of earnings or surplus of the corporation against that existing liability. They do not call it contingent. Rather, a contingent liability is the type where, oh, an action is instituted for certain damages. There, in that instance, the liability is not established. But in our case we have an existing, binding, contractual liability for repayment. The amount of payment, it is true, is uncertain, and I will certainly admit, from a sheer economic standpoint, there is a certain loss involved

because we have a non-interest bearing loan, so to speak, and economically if you loan $100 to be repaid over ten years at ten dollars a year, you have certainly made a bad investment. But of course we are concerned with the legal aspects and not the economic aspects of the case.

The Court: As I followed petitioner, petitioner was applying Burnett versus Logan to the cases of the individual stockholders upon dissolution of the corporation, and wasn't referring to it with respect to the effect and nature of a payment in the first instance by the corporations to the water company. I don't know whether I follow you or not, because you haven't divided the two too definitely.

Mr. Constable: I have, your Honor, been directing [28] my attention until this point to the matter of inclusion of these costs in the cost of goods sold.

The Court: I see. All right. Now, what about the individual stockholders?

Mr. Constable: At that point I may say that the petitioner is correct, that the respondent's determination of the fair market value of the contracts to the individual stockholders is approximately 50 percent of what is the remaining face value of the contracts at the time of dissolution. In other words, the respondent has taken the initial deposit, deducted what has been refunded, which gives the remaining amount which can be recovered.

The Court: Some of the amounts paid already have been recovered at the time of dissolution?

Mr. Constable: That is correct.

The Court: I hadn't heard of that before. On what basis were they paid back?

Mr. Constable: Well, our stipulation of fact is very lengthy on that point. It goes into all of the refunds that were made and the dates that they were paid.

The Court: Just generally why were they paid back?

Mr. Constable: Well, your Honor, people moved into the homes and began using the water, and they paid their water bill, and the water company then refunded the deposit.

The Court: You mean some of them had used it?

Mr. Constable: That is correct. [29]

The Court: The anticipated amount or required amount of water within the two-year period, or was it just ratably refunded?

Mr. Constable: No, your Honor, the full amounts were not repaid.

The Court: I understand that, that is, the full amount that the corporation paid out. But was it a pro rata part or what, according to the use of water, or what?

Mr. Constable: Well, your Honor, the contracts provided that the water company will repay this deposit on the basis of one-third or in some contracts 35 per cent of the gross revenue that it receives from these particular water users.

The Court: And then have to wait until the end of the ten-year period?

Mr. Constable: No.

The Court: Or till enough water was used to cover the full amount?

Mr. Constable: That is correct.

The Court: I see.

Mr. Constable: It may be well at this point to give what I think is perhaps one of the critical clauses in these contracts. There are several, and I will select one that I think is typical.

For the sum of $14,000, the deposit, the water company agrees to extend pipe lines for the service of water to the [30] petitioners' tracts, and going on, "* * * Refunds of the sum advanced will be made in the amount of 35 per cent of the gross revenue derived."

I might say, your Honor, this is a contract now between the water company and the builder.

The Court: Yes.

Mr. Constable: "Refunds of the sum advanced will be made in the amount of 35 per cent of the gross revenue derived from the sale of water to occupants of said subdivision for a period not to exceed ten years from the date of completion of the main extension. Refunds shall cease at the time the entire amount has been repaid should this occur prior to the expiration of the said ten-year period."

The Court: In other words, as water was used they immediately started getting part of the money back, is that correct?

Mr. Constable: That is correct, your Honor. Now, there is in each instance an understandable lag between the period that the deposit was made

and which refunds came in because the installation of the water mains is one of the first things done in a subdivision, and the deposit was made when the mains were installed, so there naturally was a lag during which time the homes were built, sold, and the people moved in and started using water.

The Court: How did the petitioner treat those [31] amounts that they get back?

Mr. Constable: Well——

The Court: In these years?

Mr. Constable: We have stipulated to that too. While the corporations were in existence, they picked up these refunds as a credit to their cost of houses sold.

The Court: They entered the amounts paid to the water company on their books as part of the cost of houses sold?

Mr. Shearer: That is correct.

The Court: And then credited this back as a recovery on that, is that correct?

Mr. Constable: That is correct. Now, after the corporations were dissolved and the contracts were in the hands of the stockholders, the stockholders—none of them—reported any of the refunds as income until in about December, 1952 or January, 1953 they filed amended returns for the year 1951 and picked up all the refunds that they had received to December 31, 1951.

The Court: What are our years?

Mr. Constable: Our year on the stockholders with regard to the valuation is 1950.

The Court: 1950?

Mr. Constable: Yes.

The Court: What are the years for the corporation?

Mr. Constable: There are varying dates, your [32] Honor, running from June 30, 1950—I am giving you now the last fiscal period—June 30, 1950 to December 31, 1950.

The Court: All right.

Mr. Constable: Within the last six months of 1950.

Now, I think at this time, your Honor, while I am on the matter of water contracts, our pleadings in many instances, many of the dockets refer to these refunds as contingent, and I have talked with Mr. Shearer and he has no objection, and informed me that it will not make a material difference in his case if I be permitted to amend certain sections of our answers by merely striking the word "contingent." I can read those docket numbers and paragraph numbers into the record.

The Court: You better do it.

Mr. Shearer: Perhaps counsel's statement to me, to which I answered "Yes", was not audible. I said, "I have no objections."

Mr. Constable: Then I will move to amend the respondent's answer by striking the word "contingent" as it appears in the following paragraphs of the following docket numbers:

Docket 51231, paragraph 5 (e), 51232, 5 (e), 51234, 51235, 51236, 51237, 51238, paragraph 5 (f) for all those dockets. Docket 51239, docket 51240, 51241, 51242, paragraph 5 (e), for all those dockets.

51226, paragraphs 5 (j), 5 (v), 5 (x), 5 (hh), 5 (rr), 5 (tt), docket 51228, paragraphs 5 (k), 5 (w), 5 (y), 5 (ii), 5 (ss), 5 (uu); 51229, paragraph 5 (k), 5 (w), [33] 5 (y); docket 51230, paragraph 5 (e); 51233, paragraph 5 (f).

That is the end of my motion, your Honor.

The Court: The motion will be granted.

Mr. Constable: Now, your Honor, with the Court's permission I will leave the matter of includibility of these deposits into cost in the individual stockholders' cases with regard to the valuation problem of the water contracts; as was stated, respondent discounted the remaining face value at the date of dissolution to 50 per cent, approximately, and determined that that was the fair market value.

The Court: What effect did he give that in his determination of deficiency and inclusion of income?

Mr. Constable: Those items were then included as long-term capital gains.

The Court: As part of the property value received upon dissolution of the corporation in exchange for the stock?

Mr. Constable: That is correct, your Honor.

The Court: All right.

Mr. Constable: In the valuation case, again, your Honor, I feel that if the corporation cases fall with regard to the inclusion of the deposits in their cost, it probably will be that, that is, if those parts are includible in their costs, then I think we will still have the issue of valuing what

remains of the contracts to the stockholders. I think that is unquestioned. There is no doubt about that. [34]

That is all I intend to offer in my opening statement on the water contracts unless the Court wishes to hear more.

The Court: Well, I want to ask counsel for the petitioner: The respondent in his determination, as I understand it, has placed the amount in computing the receipts from liquidation of the corporation in respect to these water main matters at 50 per cent?

Mr. Shearer: Yes, your Honor.

The Court: Now, assuming that the Court concludes that the argument or contention relying on Logan versus Burnett, and Westover versus Smith, is not well taken, is the petitioner contesting the 50 per cent determination?

Mr. Shearer: We are not conceding it, your Honor, but we recognize we will not have met our burden in overcoming——

The Court: You what?

Mr. Shearer: We do not concede it, but we recognize that we will not have met our burden in connection with the presumption.

The Court: All right. In other words, you don't intend to put on any proof?

Mr. Shearer: Not valuation with respect to that point.

The Court: All right. You may go ahead, Mr. Constable. [35]

Mr. Constable: The stipulation of fact. I think,

trims the issues down very clearly. Giving the Court an example, we have taken each docket and specifically outlined what there remains for the Court to find in that particular docket.

That is all I have with respect to the corporation dockets.

I might touch on the excess profits problem. I think there the particular law involved is not so much a rate as it is a ceiling on a rate, and Congress intended to take new corporations and as they came into existence, fulfilling certain qualifications as a new corporation, then to give them a ceiling on their excess profits tax, and if they came into existence during the period between about '45 and '50, with certain other qualifications they then could become new corporations. And if they were one year old, the ceiling was 5 per cent. If they were two years old, it is still 5. If they are three years old, it goes up to 8, and if they are four years old the ceiling is 11, and at five years old it goes up to 14 per cent.

The issue involved was, was Lawrence Land Company a second-year corporation or a fourth-year; that is, was it two years old or four years old. Respondent is contending that it is four years old and hence entitled to only a higher ceiling.

The Court: It was actually organized——

Mr. Constable: It was actually incorporated in March of '49. [36]

The Court: And had been in existence in this taxable year; it was in its first year, is that the idea, as far as that corporation itself is concerned?

Mr. Constable: Your Honor, the period involved for Lawrence is March 1, 1950 to December 31, 1950.

The Court: I see.

Mr. Constable: The corporation was formed in March of '49.

The Court: I see.

Mr. Constable: Now, the law also provides that where we have common control of several corporations, it can be that, as for example here, Lawrence, if Whittier and Richard and Rex, the other corporations are similarly controlled by the same parties, then it may be that if these corporations are engaged in a trade or business substantially similar to the trade or business of the taxpayer corporation, then the formation date of the earliest of the corporations will be used in determining what ceiling on the excess profits tax is applied.

The Court: Yes.

Mr. Constable: And the facts, I don't think they are in dispute. On this issue I frankly am not too clear on what Mr. Shearer's position is. I think he is probably going to argue the matter of law.

The Court: He had some reference to Richard, but I was never able to understand what it was.

Mr. Constable: Well, your Honor, I believe the issue is in relation to Lawrence, Docket 51233.

The Court: That is right. But in connection with that he was referring to Richard. Now, just what the reference was, I don't know.

Mr. Constable: His reference there, I think the evidence will show, from the stipulation of facts,

that Richard was incorporated back in July, July 10, 1947 and commenced doing business on about that date. So that respondent has made the determination that, because Richard was—began in '47 and because Richard and the other companies were commonly owned and in a similar business, then Lawrence is a four-year-old corporation.

The Court: I see. That was respondent's determination?

Mr. Constable: That is correct, your Honor.

The Court: All right. And he was contending that Richard's period of existence has no applicability to Lawrence for the purpose of this provision of the statute?

Mr. Constable: Well, as I take it now——

The Court: We will ask him. Is that right?

Mr. Shearer: My position is that it depends on what Congress meant by the word "similar."

The Court: I am not asking you that. I understand that. But your position actually is that Richard doesn't control Lawrence? [38]

Mr. Shearer: No, no. I was narrowing the definition of the issues simply to the word "similar" because we have conceded that Richard was earlier incorporated and that the controlling factors existed, and their only escape is the similarity of business.

The Court: Well, I don't know why you resist the simple statement of matters, but if the statute and the interpretation of the statute and the word "similar" is as respondent contends, then do you concede——

Mr. Shearer: We concede, yes.

The Court: Concede?

Mr. Shearer: Yes.

The Court: But in the situation you contend that the statute is not read that way and thereby Richard has nothing to do with Lawrence?

Mr. Shearer: Yes, your Honor.

The Court: That is all I was asking.

Mr. Shearer: I'm sorry. I think the word "controlled"——

The Court: I wasn't asking anything about whether you were right or the respondent is wrong on the interpretation of the statute. I was just trying to get the point of dispute.

Mr. Shearer: The word "controls" happens to be used in that particular section, and I now see that your Honor was referring to control in a different sense when he directed his question. [39]

The Court: I wasn't referring to control at all. I was assuming a situation one way and then the other so I could understand what your differences were. All right, anything more on that point?

Mr. Constable: No, your Honor. That I think winds it up.

The Court: Now, unless there is something else relating to the corporation you better give me the respondent's position about the issue in the—what is it—the Gersten case, on the divorce and remarriage and joint return question.

Mr. Constable: Well, respondent's position on that one, your Honor, is very simple: I think we can show on brief—I have been unable to stipulate

with petitioner—that the divorce and marriage in Mexico were invalid in California. Respondent's position is that the petitioner was not married to this woman for purposes of filing his Federal income tax return at the end of 1950.

I think petitioner's statement that the Government should not intrude into the matrimonial questions is entirely incorrect because the statute places a tremendous burden on the respondent to determine just who are entitled to file under the joint return provisions.

The Court: That is based on whether they are married or not at the end of the year, isn't it?

Mr. Constable: That is correct, your Honor. [40]

The Court: That is a Federal statute?

Mr. Constable: Yes. We have stipulated that the parties to that Mexican marriage and divorce were residents of California during 1950. I would like to offer to stipulate that they were also domiciled in California.

Mr. Shearer: I think without question they were.

The Court: All right.

Mr. Shearer: So stipulate.

Mr. Constable: In regard to the transferee payment, that is in Docket 51227.

The Court: Is that the one where there was a question about the deductibility for interest?

Mr. Constable: That is correct, your Honor.

The Court: Well, I think the petitioners' counsel referred to the proposition——

Mr. Constable: I am trying to locate the 90-Day Letter.

The Court: Oh, I see. Do you have that docket number?

Mr. Shearer: That is, the first docket?

The Court: 51227.

Mr. Shearer: 26.

The Court: 27.

Mr. Shearer: Oh, 27 then.

Mr. Constable: In that issue petitioner and Robbins [41] were involved in litigation wherein they were alleged to be transferees of a certain organization, and it seems that petitioner Gersten made a payment in connection with that transferee liability. Now, in 1949 when the payment in question was made, we have stipulated that at a certain date the other party, Robbins, was insolvent. And so respondent determined that half of the amount paid by petitioner Gersten was a non-business bad debt which is to be treated as a short-term capital loss.

Now, that particular amount, for example, the payment was forty-seven hundred odd dollars. Respondent determined that half of that belonged to Robbins, was Robbins' liability, paid by petitioner Gersten when Robbins was insolvent. Therefore, half of the $4,700 $2,300 is a non-business bad debt of petitioner Gersten, and to be treated as a short-term capital loss.

Now, with regard to that part of the $4,700 which applied to petitioner Gersten, respondent held that that part of it which related to other than interest

in the payment, which was $1,700, is a long-term capital loss, and treated it accordingly; and that the difference between petitioner Gersten's one-half of the $4,700, which was $2,300, the difference between the $1,700 which respondent treated as a long-term capital loss and the $2,300, or 630, which was interest, was allowed as a deduction for interest paid. Now, that's the basis. [42]

The Court: Respondent didn't allow the portion of the interest that was applicable to the other man's part of it, did he?

Mr. Constable: No, your Honor. Respondent took the entire amount, the entire one-half applicable to Robbins, and treated it as a loan to Robbins and as a bad debt and treated it as a short-term capital loss.

The Court: Well, you gentlemen are going to have your work cut out for you on briefs on that point because, whereas it didn't used to make any difference, now with all the scrambling over capital treatment, capital gains and capital loss treatment, a lot of new contentions and some new philosophies are creeping in.

The one comparable situation, early, was the matter of bank stock assessments, where a bank went insolvent; originally it didn't make too much difference. Even though everything was gone, they didn't have anything left when the assessment was paid. It was a loss and that was that. In more recent years there has been quite a scramble over whether or not that should be treated as part of the cost of stock when, as a matter of fact, they

knew when they were paying it they weren't acquiring anything, because what they were supposed to be acquiring was already gone. We have had cases on that from that angle, and my recollection is that Murphy group, I believe, and some others about that time; we held that cost of stock. [43] On the other hand, in the case of a deceased potential debtor in the Agnes Fox case, the Second Circuit was of a view that since the man was dead and the payment was a payment after secondary obligation, that it was a payment to protect property and was a loss, and came under that provision of the statute and not under the theoretical, arising from a debt and a bad-debt loss.

So as to just where the courts are going to come out and what is going to be settled law on it, I am frank to say I don't know as yet, so you gentlemen will be expected to enlighten the Court with everything that there is on it, in this modern attitude, that is, the current attitude toward these questions.

Mr. Constable: Now, in Albert Gersten 51226 there is a point there I think we should mention, your Honor. The parties have agreed to do something that, in their stipulation, I am not sure we can do without permission of the Court.

In the stipulation, paragraph 57, we say that petitioner reported his one-half interest in land received from the liquidation of Rex Land Company, referred to herein as paragraphs 36 and 37 of the fair market value of $118,000. Now, this land is something that was distributed to the stockholders at the time of dissolution of one of these corpora-

tions, Rex, in addition to the contracts that were distributed. Now, the value of 118,000 was reported. The notice of deficiency does not disturb that valuation and the petition doesn't disturb [44] it. However, we are agreed in our stipulation to change it; that is, we are agreed to raise the issue, to allow the issue to be raised, decrease the valuation to $107,675. In other words, we are raising the issue and then agreeing on it, and I am not sure whether we need the Court's permission or not. It is something that will, if granted by the Court, be taken into account under Rule 50.

The Court: I don't see what the Court has to do about it, if you fellows agree that that is what it is.

Mr. Constable: My point was, the issue has never been raised and we wanted to make clear that we are making it part of the——

The Court: I would have no problem about it.

Mr. Constable: That problem is also common in 51228.

The Court: Particularly since you say you have raised it and agreed on the disposition of it.

Mr. Constable: That is correct, your Honor.

The Court: All right.

Mr. Constable: Now, in the stockholders' dockets, 51226, 51228, 51229, there is a little tag end that hasn't been agreed upon, and I think Mr. Shearer will stipulate that in the notice of deficiency, page 3, attached to the petition in Docket 51226 the determination relative to the refundable deposit of $378 in item 2, and the determination as to the

value of a State tax claim of $126.80 in item 3 are conceded [45] by the petitioner.

Mr. Shearer: Yes, your Honor. But let the record be clear that that refundable deposit has nothing to do with the payment in connection with the San Gabriel. That phrase has been used before in connection with that.

The Court: All right, the record will show the agreement.

Mr. Constable: In Docket 51228, referring to the deficiency notice attached to the petition in that docket, page 4, respondent offers to stipulate that petitioner concedes the refundable deposit item of $378 and the State tax claim item of $126.80 referred to in item A on page 4.

Mr. Shearer: So stipulated.

The Court: That is comparable to the other one?

Mr. Shearer: Yes, your Honor.

Mr. Constable: In Docket 51229, similarly, respondent offers to stipulate that in the notice of deficiency attached to the petition in that docket, page 2, the determination with regard to the refundable deposit of $189 in item A is correct.

Mr. Shearer: So stipulated.

The Court: All right.

Mr. Constable: Now, your Honor, I have another little item. Respondent offers to stipulate that on or about March 13, 1950 a contract marked Exhibit 4 was entered into between Whittier Development Company and San Gabriel Valley Water [46] Company which concerned the installation of water

pipe lines to tract No. 14001. This contract is referred to on the books of the water company as Job No. 603W, and that a transcript of the 241 ledger of the San Gabriel Valley Water Company for Job No. 603 W is as shown on what is marked Exhibit 8.

That is the end of the offer to stipulate.

Mr. Shearer: In that connection, your Honor, I will, subject to the language that appears at the beginning of the written stipulation, reserving the right to object to the materiality, join in the stipulation.

The Court: In other words, you agree to the correctness of it but reserve the right to object on the ground that it is immaterial?

Mr. Shearer: Yes, your Honor.

The Court: Very well.

Mr. Constable: Your Honor, it may be that in brief the parties or one of them may wish to argue in terms of present values of annuities. For the record I would like to make an offer to stipulate to Mr. Shearer very briefly on the present value of an annuity subject to his checking it later.

The Court: What do annuities have to do—you mean present value of a dollar on a given date?

Mr. Constable: The present value, your Honor, of an annuity payable over a period of, say, nine years.

The Court: Well, go ahead with your statement.

Mr. Constable: Respondent offers to stipulate that the present value of the dollar per annum for a period of nine years, based upon interest earn-

ings at the rate of 5 per cent, is $7.108, and the present value of 70 cents per annum for a period of nine years at 5 per cent interest is $4.97. The offer to stipulate is made into the record for the purpose of encouraging counsel for the petitioner to, at a date subsequent to trial and before briefs, agree on this present value or other present values.

That is the end of the offer to stipulate.

Mr. Shearer: I would like to reserve answer. I am not prepared to make that stipulation at this time. I am not sure——

The Court: I think you better get together and let's get it settled one way or the other by the end of the trial.

Mr. Shearer: I think so, your Honor.

The Court: All right.

Mr. Constable: One matter, your Honor: I don't know yet whether I am going to be required to call an expert. I don't think so and I hope not.

The Court: What does that have reference to?

Mr. Constable: Well, your Honor, there has been some reference made that we can finish this case today, and I think we may be able to. However, my expert can not be here until Monday. [48]

The Court: I won't have any room for him Monday. I might have room for him tomorrow if we have to.

Mr. Constable: That would be agreeable with me if it would be agreeable with Mr. Shearer.

Mr. Shearer: It is agreeable with me.

The Court: We will have to see what the situation is. What do you want an expert for?

Mr. Constable: Your Honor, as my case stands, I don't think that I will need one, but I don't know what Mr. Shearer is going to do.

The Court: What is it you are going to value?

Mr. Constable: I am going to attempt to value nothing, because we have our presumption, of course. But I don't know what Mr. Shearer is going to offer.

The Court: Let's cross the bridge when we come to it.

Mr. Constable: Very well.

One remaining item in, for example, Docket 51228 at paragraph 5 (h). Well, I think, your Honor, in view of the discussion with counsel, that my remarks just made with relation to Docket 51228 can be stricken.

The Court: All right.

Mr. Constable: We prepared about 80 paragraphs of facts, your Honor, and I forgot the simple fact of putting in the returns. At this time I would like to stipulate that the [49] returns for the individual petitioners may be received into evidence as follows: Albert Gersten, Lucille Gersten, 1949, Exhibit Q; Albert Gersten, Bernice Ann Gersten, 1950, Exhibit R; Myron P. Beck and Ann H. Beck, 1949, Exhibit S; Myron P. Beck, Ann H. Beck, 1950, Exhibit T; Milton Gerston and Mary Gersten, 1950, Exhibit U.

That is the end of that offer to stipulate. Is that so stipulated?

Mr. Shearer: I so stipulate. Because I don't

know the purpose of the proposed Exhibit S, I will reserve the right to object to its materiality.

The Court: All right.

Mr. Constable: S is a return for the year in which a determination is made, your Honor, but not contested.

The Court: I see.

Mr. Constable: Another offer to stipulate: Respondent offers to stipulate that on or about January 20, 1953 petitioners Albert and Lucille Gersten and petitioners Myron P. and Ann H. Beck signed consents extending the period of limitation upon the assessment of income and profits tax for the year 1949 to June 30, 1954.

Mr. Shearer: So stipulated.

The Court: Very well.

Mr. Constable: That is all I have, your Honor.

The Court: We will adjourn until 2:00 o'clock.

(Whereupon, at 12:45 p.m. a recess was taken until 2:00 p.m.) [50]

Afternoon Session. 2:00 P.M.

The Court: Proceed.

Mr. Constable: May I have just a moment for some details?

The Court: Yes.

Mr. Constable: First we have a stipulation of fact which I will offer for filing.

The Court: The stipulation will be received and made a part of the record.

Mr. Shearer: If your Honor please, in connection with the stipulation of facts, by its terms, the

stipulation reserves the right to object to materiality of any fact herein stipulated.

Now, the difficulty here is the time of making such objection. It may well be that, and I can conceive even the probability, apart from this possible expert, that respondent will simply rest with the stipulation. For that reason I thought perhaps if I indicated the particular portions of it to which I did wish to object on the ground of immateriality, at this time——

The Court: Oh, yes, any objections to any part of it on any such ground, you make the objections and we will take a look at them now and clear the record on them.

Mr. Shearer: My objections are substantially all of the same kind and they go to paragraph 7, 8——

The Court: All right.

Mr. Shearer: If I may, I will enumerate the other paragraphs which are all a similar type of paragraph: 7, 8, 20, 30 and 41; and also the exhibit which counsel put in on oral stipulation. I don't know what letter was assigned to that—Exhibit 8. Now, I might clarify this by stating that, for the purpose of the individual cases, I can see where certain of the payments made—I'm sorry, I said "individual cases;" I meant corporate cases. In connection with the reflection of income of those corporations, the payments made prior to their dissolution would be material, and my objection does not run to those items. However, the entire list is compiled as a single list for convenience, with the understanding that that convenience would not preju-

dice my objection. I can enumerate the specific points from which my objection runs or I can state it in general, that all payments made—I object on the ground of immateriality to the receipt into evidence of all payments made subsequent to the dissolution of the corporations.

The Court: I think I had better get an explanation of these accounts. The paragraphs mentioned appear to be transcripts of ledger account in the books of the water company.

Mr. Shearer: Yes, Your Honor.

The Court: And I would like to have some explanation of these entries in this account as to what they are per [52] books.

Mr. Shearer: If I follow Your Honor, I might say that the column "Credits" represents an amount equivalent to that originally paid to the water company. The column entitled "Charges" represents the payments made by the water company to the subdivider or to the owner of the contract, as the case may be, if the contract were assigned. The balance is simply a mathematical subtraction of the amount paid from the next preceding balance.

The Court: Let me get at it this way: Is it a proper interpretation to say that the first one, being in paragraph 7, the account being, as I understand, credited to Job No. 363W?

Mr. Shearer: Yes.

The Court: That job, which was the construction of water mains up to one of these subdivisions by the water company, was credited with the payment of 23,764?

Mr. Shearer: Yes, Your Honor.

The Court: And then that was charged out, leaving balances as payments were made back over the period of time and as the water was used by the tenants, is that right?

Mr. Shearer: Yes, Your Honor. I may say that the date reflects the date of payment by the water company and not the dates——

The Court: The amounts under "Charges" so that the over-all situation is that in terms of water companies the way [53] one interpretation might be, that it was charging itself with 23,764 and was reflecting satisfaction of that by these various payments on the dates mentioned, leaving the balance as shown in that particular one at December 1954 at 12,999.26.

Mr. Shearer: That would be an interpretation on the basis of the information to this point. It is my understanding, and the evidence, I believe, will show, that they set these up as what they called contingent liabilities, and I don't want to lose sight of that fact.

The Court: I am not trying to get any admission or statement here which by way of impingement overcomes the contention that you are making in the over-all case. I am just trying to get a fair reading of the Act as it is carried by the water company without regard to whether that would be or indicate a proper legal result as between the water company and these individuals or the company or not. The remaining question that comes up,

and which might be one that when a consideration of the proper treatment of such an account is given, would be what would be the entry in an account such as this on the books of the water company if, after ten years had run from the opening—and that was November 21, 1947 I believe in that particular one——

Mr. Shearer: Yes, Your Honor.

The Court: If, at the end of ten years, say, the balance column showed a $3,500 balance in there?

Mr. Shearer: Well, I don't wish to give evidence from the counsel table, but the evidence, I think, will show that that is put into what is called a donations account.

The Court: On the books of the water company?

Mr. Shearer: Yes.

The Court: At the end of that time they would clear this account by taking the balance somewhere else?

Mr. Shearer: Into a donations account, and the reason, they use that phrase as meaning in relation to the requirements of the California Public Utilities Commission, of the treatment of that amount as allowed capital or whether they are entitled to return of it for the purpose of rate-setting and so forth, and therefore it goes into what is called a donations account. And without question at that stage, there are absolutely no rights which the subdivider has in the——

The Court: I understand.

Mr. Shearer: On the other hand, the water com-

pany is required to keep that separately in order for another purpose, that is, the purpose of rate setting.

The Court: Might become of some interest directly or indirectly as to how it is treated in making out the income tax return. So I merely mention that at this stage because the Court may have to face some consideration of that proposition in reading this stipulation. So you will bear that in mind, and if it is regarded by counsel as requiring any [55] consideration or being dealt with in the course of the trial, you may do so; and after that, on briefs, if it is regarded as material.

Now, you object on the ground of immateriality, and what is the basis of the claim that it is immaterial?

Mr. Shearer: The issue here, Your Honor, relates to what is to be done with respect to the payment in the year in question. All entries, for example, in paragraph 7, all entries subsequent to the entry under date of 6/14/1950 relate to transactions which do not affect—I shouldn't use that—which do not at least directly affect on the books of the company, which is no longer in existence, its income or outgo.

Now, what its stockholders subsequently receive, we submit, is not material and has no relationship —can not affect the right or the lack of right of the company to treat this payment as a cost of goods sold, and for that reason the evidence does not tend to prove or disprove any of the matters in connection with this issue.

It is my understanding that this is not offered with relation to anything but the corporate issue.

The Court: Well, it is in here as a fact, and I think that, rather obviously, certainly, up through these tax years that are involved, there can be no question that it is material. Now, there might be some question as to the weight that is to be given to it in arriving at the question as to [56] the proper effect on income and arriving at net income of these petitioners. But I think that certainly up through these taxable years the contention that it is immaterial is not well taken, and in any event I will overrule the objection.

Mr. Shearer: I conceded up to the years in question.

The Court: Well, the objection will be overruled.

Mr. Shearer: I will enumerate other paragraphs that have the same language relating to the different taxpayers: 12, 23, 34, and 44. I have no objection. I simply wish to call the attention of the Court to the fact that the conversation this morning, the discussion this morning brought to my attention that perhaps the use of the word "deductibility" might appear to have a technical meaning in paragraph 12. That was not our intent.

The Court: A very unfortunate selection of a word.

Mr. Shearer: Yes, and that was——

The Court: In the light of the statement of the issues.

Mr. Shearer: Yes, Your Honor, and that of course is what caused me to mention it.

The Court: All right. As I understand it, then, the parties would have me read it as a question as to whether or not it is to be taken into account in determining cost basis?

Mr. Shearer: Yes, Your Honor. [57]

The Court: To the corporate taxpayer, because I don't understand the claim of deductions is being asked here.

Mr. Shearer: That is right.

The Court: All right.

Mr. Constable: May I inquire of the Court, what the Court is referring to in "cost basis"?

The Court: Well, this 12 has to do with the amount paid by J. Richard Company to the water company for running water pipe lines into this development, and there is an indication in the use of the term "deductibility," and if that were, the question were whether or or not it was an item of deduction under the statute in arriving at net income —and I don't understand that there is any such claim on the part of the petitioner at all—a deduction is a matter of legislative grace covered by Section 23 of the Code of 1939, whereas a matter of cost goes into the basis in arriving at the amount of gain that is to go into gross income under Section 22 of the Internal Revenue Code of 1939; a wholly different thing. And the word "deductibility" is very bad to use it in that sense because of the confusion that it does give rise to. And it is rather amazing to me the number of times that I find where it is loosely used. It is always well to avoid the use of a word where, under the Code or statute

to be applied, it has its own special statutory meaning. And I am glad that attention has been called to it, because we will read it in light of the [58] statement of the issue here.

Mr. Shearer: Is that satisfactory?

Mr. Constable: Yes. I might add, paragraph 72 sheds some light on that.

The Court: If there are any others I think it would be well to——

Mr. Shearer: I enumerated the other paragraphs.

The Court: All right, you may proceed.

Mr. Shearer: Mr. Moseley, please.

Mr. Constable: May I continue? I had another item.

The Court: All right.

Mr. Constable: This morning certain returns were stipulated into evidence, marked Exhibits Q, R, S, T, and U. The Clerk has asked me, for the record, to hand them to him for marking.

The Court: All right. When they are offered, they will be given the designations indicated.

The Clerk: Q through U in evidence for the respondent.

(Respondent's Exhibits Q through U were marked for identification and received in evidence.)

Mr. Constable: And the same applies to what was stipulated this morning as Exhibit 8.

The Clerk: Exhibit 8 for the petitioners. [59]

(Petitioners' Exhibit No. 8 was marked for identification and received in evidence.)

Mr. Constable: This morning, in offering to stipulate the consents for Albert and Lucille Gersten and Myron P. and Ann H. Beck, counsel inadvertently forgot to assign respective exhibit numbers. I will hand the consent of Albert and Lucille Gersten to the Clerk to be marked V.

The Clerk: Exhibit V for respondent.

(Respondent's Exhibit V was marked for identification and received in evidence.)

Mr. Constable: And Beck, to be marked W.

The Court: Very well.

The Clerk: W.

(Respondent's Exhibit W was marked for identification and received in evidence.)

Mr. Constable: Your Honor, is it in order to move that the cases be consolidated? I am not sure that we have——

The Court: I am regarding them as consolidated for the purposes of the proceeding here.

Mr. Constable: Your Honor, I think I will wait until we conclude before proceeding to ask for permission to withdraw all the various exhibits.

The Court: Very well. [60]

Mr. Shearer: Mr. Moseley, please.

M. E. MOSELEY

was called as a witness by and on behalf of the petitioners, and, having been first duly sworn, was examined and testified as follows:

The Clerk: Tell us your name, please, Mr. Witness.

The Witness: M. E. Moseley.

Direct Examination

Q. (By Mr. Shearer): Will you state your occupation? A. I am an engineer.

Q. What is your present employment?

A. I am vice-president of San Gabriel Valley Water Company.

Q. Are you also the general manager of that company? A. Yes, sir.

Q. How long have you been with San Gabriel in an executive capacity?

A. With San Gabriel and its predecessor, since 1937.

Q. Is San Gabriel a private corporation?

A. Yes, public utility under the California Public Utilities Commission.

Q. I show you Exhibits 1 through 7, inclusive, which are water contracts, apparently executed by you on behalf of San Gabriel. Are you familiar with those? [61] A. I am.

Q. Now, did you negotiate those particular contracts with the respective subdividers?

A. I did.

Q. Did you participate in the fixing of the amount called for which the respective contracts

(Testimony of M. E. Moseley.)

called for payment to San Gabriel? A. I did.

Q. How were those amounts arrived at?

A. The amounts represent the cost of the facilities which are required to be installed, and the facilities that are required are determined by the water company after an engineering study.

Q. Are you generally in charge of negotiating that type of contract for San Gabriel?

A. Yes, I am.

Q. Approximately how many of such contracts have you worked on and seen in connection with your employment?

A. That is difficult to say. It is a great number. It might be 500 or perhaps a thousand.

Q. Do those contracts always contain what I will call a refund provision? A. Yes, they do.

Q. The language you will note is somewhat different in each of the contracts, but the substance is the same. Is [62] there any reason why the refunds and their rates are more or less uniform in the various contracts?

A. Well, the contract and the refund rates are prescribed by the Public Utilities Commission. They have prescribed changes in rules from time to time.

Q. And each of those contracts, then, conformed to the rules then existing at the time of the California Public Utilities Commission?

A. That is correct.

Q. Now, who actually makes the water pipe installation?

(Testimony of M. E. Moseley.)

A. The water company does, or it employs a contractor to do it under its direction and supervision.

Q. The subdivider has nothing to do with it beyond the payment, is that correct?

A. That is correct.

Q. Now, are these pipe lines generally installed in that portion of the subdivisions which are dedicated to public streets? A. Yes.

Q. Is that true in the specific subdivisions referred to in contracts which are Exhibits 1 to 7?

A. I think that is true with the exception of minor instances.

The Court: Are you talking about the connections and the lines after they reach the subdivision?

The Witness: Yes, within the subdivision. [63]

Q. (By Mr. Shearer): The water mains actually are laid in the subdivisions themselves, are they not?

A. Yes, a subdivision consisting of lots and streets.

Q. And they are generally, in this case you said except for minor instances, in the street portion of the subdivision? A. That is correct.

Q. You do not have anything to do with the connection from that water line to the house itself?

A. Yes, we extend a connection from what are commonly called water mains to a meter box, which will be near or at the property line, the property line being the limits of the public street.

The Court: Right at this point let me see if we can clear up one matter, since it is a matter that

(Testimony of M. E. Moseley.)

I don't think there should be any dispute about, and maybe we can clear it up by mentioning:

Now, am I to understand that in these four instances that the water lines or mains, the cost of which is here involved, are the lines or mains that are within the confines of the subdivision, or does it likewise involve, for instance, if an existing water main runs within a quarter of a mile of a subdivision, that part of the main which it takes to run that quarter of a mile before it reaches the boundary of the subdivision? Do we have one or both or none of those? [64]

A. Well, the one we are just discussing certainly is an important element in the cost of the installation. A subdivision may be started, and it may be fortunate and have a water main entirely along one frontage. It might not have any internal streets at all.

The Court: Might not have what?

The Witness: Any internal streets. A piece of land might be subdivided with a pipe line already alongside of it. Off-site distance certainly has a good deal to do about it. The particular layout of the subdivision has a great deal to do with it, from an engineering standpoint, in determining the size of the pipe lines that are involved.

Q. (By Mr. Shearer): When you speak of layout, would that include the width of the streets?

A. Yes.

Q. Would that have any bearing upon the cost?

A. Well, our company doesn't lay—lays two

(Testimony of M. E. Moseley.)

pipe lines on a street, if the street exceeds 70 feet in width, one on either side.

Q. Now, would the pattern of the layout of streets within the tract have any bearing upon the cost?

A. Yes. Am I supposed to continue? Did you ask me a general question?

Q. Yes, if you would have other factors, if you would [65-66] simply give them to us.

A. Other things that would be considered from an engineering standpoint are soil conditions, the type of pipe that would be laid to fit, suitable for those soil conditions, which then revolves into—is an element of cost, finally.

Q. Will you explain that a little?

The Court: Let me ask a question right there, because I don't know that I follow. You say "from an engineering standpoint." Are you using that as something distinctive and different from cost standpoint? When you speak about "engineering standpoint," are you talking about cost?

The Witness: I think cost follows the engineering.

The Court: I just want to know what you mean, is all I want to know, because you seemed to be very carefully referring to it in your answers, to matters from an engineering standpoint, and I think that, primarily, the question here is directed to cost.

The Witness: All right. I think I know what you mean. From a long-range cost standpoint, it

(Testimony of M. E. Moseley.)

would not be good engineering to put in a pipe line which will not survive in a particular soil, and it might be well from a short-range standpoint to put in a pipe line which wouldn't stand a particular corrosive soil condition, but in long-range cost you must fit the material to the conditions you have, and some of those are different. [67]

The Court: Now you are bringing in another matter that I don't know what you mean, when you are referring to "from an engineering standpoint", and now you are talking about a long-range cost standpoint.

Q. (By Mr. Shearer): Who determines what kind of pipe materials are laid?

A. The water company.

Q. And some materials are more expensive than others, are they not? A. That is correct.

Q. In given cases do you determine whether a more expensive material be laid because in your opinion the particular soil will not properly take the cheaper—— A. Yes.

Q. One of the elements——

The Court: I think it would be better if you will ask him the questions instead of giving him the answer in the question.

Mr. Shearer: Yes, your Honor. I thought I understood what he had said and was trying to translate it.

The Court: Well, I believe he better translate it.

Q. (By Mr. Shearer): Of the factors you have

(Testimony of M. E. Moseley.)

mentioned which affect the cost of the installation, do any of those have any bearing upon the amount of water which is used in connection with that installation? [68] A. No.

The Court: What do you mean by that?

The Witness: Are you asking me?

The Court: Yes.

The Witness: The cost of the pipe line in front of a dwelling or lots wouldn't have anything to do with the quantity of water which an individual householder used, unless it should be that the pipe line were so small that he were unable to use the quantity of water that he wished to use and they wouldn't supply it.

The Court: In other words, it is the size of the pipe line and not the cost?

The Witness: Yes, sir; and size and cost are directly related.

Q. (By Mr. Shearer): Would the fact that a subdivision's water pipe installation cost was greater because of a long distance from the water company's then existing facilities have any bearing upon the amount of water used in that subdivision?

A. No, I don't think it would.

Q. Does the nature of the pipe materials used have any bearing upon the amount of the water used? A. No.

Q. What factors do affect the amount of water used in a given subdivision? [69]

A. Oh, size of lots, which means increased vege-

(Testimony of M. E. Moseley.)

tation around the outside of a house, weather, certainly pride of ownership.

Q. Will you explain that "weather," what you mean by the "weather"?

A. Water companies don't sell much water in cold or wet weather.

Q. Any other factor?

A. I think that's all.

The Court: You mentioned something there.

I would like for you to read back that answer.

Reporter (Reading): "Answer: Oh, size of lots, which means increased vegetation around the outside of a house, weather, certainly pride of ownership."

The Court: What do you mean by "pride"; p-r-i-d-e?

The Witness: Yes. I mean the general appearance of a neighborhood, people that live there, whether or not they use water to keep their places appearing well or whether they don't.

The Court: All right.

Q. (By Mr. Shearer): Do you find that some tracts will use a greater amount of water for that purpose than others?

A. Not tracts, particularly, but areas do.

Q. In relation to the full ten-year period involved in [70] these contracts—does your occupancy vary during the ten-year period.

A. Yes, occupancy does vary.

Mr. Constable: Your Honor, I have objected maybe a little late. I think Mr. Shearer's ques-

(Testimony of M. E. Moseley.)

tioning was directed to these contracts. I would like to know—he has talked about a thousand contracts, and then we have some contracts in issue, and I am not sure which he is talking about here.

The Court: I am not either.

Q. (By Mr. Shearer): Do you understand my question to relate generally to all of the subdivision which San Gabriel services?

A. I think it will refer to any place we serve, any tracts or any areas.

Q. Was your answer intended to reflect that?

A. That's correct.

Q. Now, speaking as of the commencement of the installation of water pipes, pursuant to any one of the contracts, Exhibits 1 through 7, or any similar contract, can you predict how much, if any, of the water pipe payments may be refunded?

A. No.

The Court: Did you ever try?

The Witness: No, I don't think I have. I have thought about it. I don't think in the strictest sense I have tried to make a prediction of what would happen in these contracts, [71] because I don't know what the subdivider is going to do.

Q. (By Mr. Shearer): Insofar as the ten-year period is concerned, that of course starts not later than the completion of the installation?

Mr. Constable: Objection, your Honor.

Mr. Shearer: This is preliminary. I am stating what is in the stipulation.

Mr. Constable: I think that some of the con-

(Testimony of M. E. Moseley.)

tracts, Mr. Shearer, read "from date of completion."

Mr. Shearer: I think I said "not later than the completion of the installation."

Mr. Constable: All right.

A. That is true.

Q. (By Mr. Shearer): There is a period between that time and substantial occupancy during which your sales of water are comparatively limited, are they not? A. That is correct.

Q. Have you found that time to vary from subdivision to subdivision? A. It does vary.

Q. Is the variance substantial?

A. Yes, it is.

The Court: You are speaking of which time? We have had [72] times that were—you said you were there from 1937. Well, certainly the experiences of most any subdivider in 1937 are quite different from his experiences after World War 2, for instance, possibly during World War 2. We have had, I rather imagine, quite a range of extremes.

The Witness: Yes, sir.

The Court: So now what are you talking about?

The Witness: Well, I am not talking about 1937. I have made some inquiry——

The Court: This better be about your experience, not inquiry.

The Witness: My own company? May I put it this way: I asked questions about the experience with our contracts of people in our accounting department within the last few days, and that is the answer I propose to give.

(Testimony of M. E. Moseley.)

The Court: You know what periods they were telling you about when you asked them?

The Witness: The contracts that they were speaking of are still on the books. They have not been cancelled because of expiration of the ten-year period. I am not familiar with the particular conditions in respect to those contracts. But I did ask as to the variance in refund rate.

Mr. Shearer: May I proceed?

The Court: Yes, go ahead. [73]

Q. (By Mr. Shearer): Has there been, commencing from say 1948, a danger of loss of occupancy by destruction of homes by reason of condemnation?

A. My company has experienced that, due to the building of freeways.

Q. You know——

A. And to the construction of a flood control project.

Q. Mr. Moseley, speaking of a period of time after June, 1949, and not later than December 31, 1950, do you know of any sales of rights to receive refunds under contracts similar to Exhibits 1 through 7 which were issued by your company?

(Question read.)

A. I know of some sales, but I can't pin them down as to the time at this moment.

Q. Do you know approximately how many sales were made, that is, that you know of?

A. I know of, I believe, four contracts that have been sold.

(Testimony of M. E. Moseley.)

Q. Now, did those relate to subdivisions which had been completely occupied, that is, were completed as far as subdivision was concerned?

The Court: Which do you mean, occupied or completed?

Mr. Shearer: Strike the question and I will rephrase it.

Q. (By Mr. Shearer): Did those refer to subdivisions in respect of which [74] the homes had been completely or substantially completely built?

A. Three of them were substantially or completely built and one was not.

Q. Can you tell us approximately how many such contracts were then existing in that period to which I have referred?

A. I don't know that these were sold during that period. They may have been sold more recently than that.

Q. My question was directed to the period.

A. I told you that I knew of the sale of four contracts, but I couldn't tell you as to the time, whether they were sold during that period or not; I can't tell.

Q. Can you tell us approximately how many such contracts you had on your books between June of 1949 and the end of 1950?

The Court: Now, before you get into that, I don't know just what you are going to ask me to find from an answer to that question. I can't tell at this stage. But if it is something that is material, and important, to your case, or you think it

(Testimony of M. E. Moseley.)

is, that is something that shouldn't be asked of this witness here, to approximate, when all you would have to do is have them check and find out what it was from the records of the company. I want to allow you all the latitude in the world in the presentation of your case, but questions like that can present a terrifically burdensome duty to the Court, in the light of some arguments that are later made. Now, I mention [75] that at this time while we are still early in this proceeding, because undoubtedly those things are a matter of record, and this witness has indicated that he worked in connection with 500 or a thousand such matters, and I just don't like to be handed such an indefinite sort of a burden, when he is just being asked to approximate something that could have been determined from records.

Mr. Shearer: I would be perfectly willing to have the witness confirm it, and stipulate. But I must say there are times when given material is not sought because it doesn't appear to be necessary, and then turns out to be advisable because of an answer a witness has made.

The Court: This is a matter that is the responsibility of an attorney in the preparation of his case.

Mr. Shearer: Yes, your Honor.

The Court: We have provision which requires counsel to go into those things ahead of trial and to get record facts.

Now, I know that you have had here a rather complicated situation in that you have corporation

(Testimony of M. E. Moseley.)

cases, you have the individual stockholder cases, and then you have little side issues of individual petitioners, and you have had, undoubtedly, a very burdensome case to work up, and I am perfectly aware, and I think you are to be commended, from your demonstration here already that you gentlemen have been working at it. But if this is important, this witness very obviously doesn't know [76] the answer to that sort of thing, other than just some approximation, when, as a matter of fact, it is a matter of record. And it is better to have it right than it is to have something indefinite that I am going to have to struggle with and don't know what the answer will be to it when I struggle with it.

Mr. Shearer: Well, unless counsel is willing to stipulate that the witness may verify the specific fact, and it may be offered, I have no way of getting the exact information at this time.

The Court: You have no way of getting the exact information at this time, apparently, because this witness indicated he doesn't know, and you are just asking him to approximate matters that are rather obviously of record with the water company.

All right, let's get back to the question.

Will you please read the question?

Reporter (Reading): "Question: Can you tell us approximately how many such contracts you had on your books between June of 1949 and the end of 1950?"

A. We had several hundred.

(Testimony of M. E. Moseley.)

Mr. Constable: Your Honor, that is rather indefinite. We have got a long period of time.

The Court: Are you objecting and moving to strike or what?

Mr. Constable: Yes, I object and move that the answer be stricken. [77]

The Court: The motion is granted.

Mr. Shearer: If your Honor will withdraw his ruling for a moment, I would like to call your attention to the fact that, in my opinion, this witness has been qualified as an expert; with relation to this specific matter, he may well be able to state unqualifiedly, and the question was so directed, "Can you state a minimum amount?"

The Court: That wasn't the question, and I don't know whether it would make it any better if it was.

Mr. Shearer: I didn't mean the minimum amount. I asked the question, "Can you state the approximate number?" And his answer related to a minimum amount, which might be helpful to the Court in trying to determine a question of four possible sales among at least several hundred.

It may be my case will be stronger if I had the exact amount and it was a thousand.

The Court: It may be, so let's get the exact amount.

Mr. Shearer: Your Honor, I have no way of getting the exact amount unless I ask your Honor to hold this matter open until Monday, which I am not disposed to do at this point.

(Testimony of M. E. Moseley.)

I have already invited counsel to stipulate with me the exact amount, and I have had no response.

The Court: I have made my ruling, so let's move on with the case, because this Court has too many burdensome matters to have to struggle over those things which are approximations [78] of matters that are of record and can be established, and I don't think it goes to the qualifications of this witness as an expert at all. It has to do with the business of this company, the business on its books.

All right, let's go on.

Q. (By Mr. Shearer): Mr. Moseley, in connection with the accounts of what is called your 241 ledger, have you seen that book? A. Yes, sir.

Q. Are you familiar with the fact that from time to time there are accounts in the 241 ledger which do not pay out prior to the expiration period? A. Yes, sir.

Q. What happens, how do you treat the unrepaid amount?

A. The amount that is not repaid is transferred to an account called "Donations in aid of construction."

The Court: Donations what?

The Witness: "Donations in aid of construction." The California Public Utilities Commission prescribed a new system and classification of accounts effective as of January, 1955. The present account, the new account for these contracts during their life is called 241; I believe the title

(Testimony of M. E. Moseley.)

of it is "Consumers' advances" or "Customers' advances for construction." The other account, into which any remaining amount goes—I don't have in mind the number—but it is still called donations, [79] as it once was. That donations account, under the present treatment, appears in the liabilities side of the ledger as a liability. The Commission treats it almost as an asset that does not exist. It is not a part of rate base, and it is now being written off like depreciation but not charged to depreciation.

The Court: In making that answer, are you talking about the way your accounts are kept for the purposes of meeting the requirements of the Utilities Commission? Is that what you are talking about?

The Witness: Yes, sir. First, there is a—federally, they are kept another way, for the purpose of Federal taxes, I believe.

Q. (By Mr. Shearer): Mr. Moseley, the change came when, did you say? A. January, 1955.

Q. '55? A. Yes.

Q. And did you not use these two new accounts prior to that time?

A. They were practically the same accounts: 241 was called 28A. I believe it has the same title, and "Donations" was 28B. I can't think——

Q. You used the word "Donations": before you used the word "Donations in aid of construction." Are you simply [80] shortening the phrase?

A. Yes.

(Testimony of M. E. Moseley.)

Q. When you said it the second time?

A. That's right.

The Court: That is the account which you carried any balance at the end of the required period, is that right?

The Witness: Yes, sir. We have taken that money and literally buried it in the ground in the form of pipe lines, and the way it is treated now by the Commission is that at the expiration of the period any unrefunded amount is actually a deduction, you might say, from the value of that pipe line.

Q. (By Mr. Shearer): When you say it isn't included in the rate base and wasn't, did you mean that it wasn't included in the rate base during the years in question here from '49, '50?

A. That is also true. It is not included in rate base.

Q. May I ask you what you mean by rate base? I don't know that this is material to our case, but you have used a phrase that I frankly don't understand.

A. Rate base is a phrase, I guess used by Commissions all over the country for the purpose of determining what assets of a company it may earn on, its fixed percentage of earnings, whatever the Commission uses.

Q. In other words, is it correct to state that they do not take into account any such unrefunded portions in determining [81] the rate of income

(Testimony of M. E. Moseley.)

you should earn on your capital investment; is that a correct statement?

A. They do not—that is correct. All unrefunded amounts, either amount that may be refunded or amounts that have gone beyond the point where there will be no refunds, are deducted from the assets of the company in arriving at a rate base.

Mr. Shearer: I have no further questions.

The Court: Any questions?

Mr. Constable: May I have just about five minutes? I think I will be very brief with this witness.

The Court: Very well. We will take an intermission.

(Recess.)

Mr. Shearer: Before counsel starts cross examination, I would like to offer to stipulate that, as of any given date, the 1950's, of counsel's choosing—and I would suggest July 1st of 1950 as being a mean in connection with these cases—that San Gabriel had in effect a given number of contracts similar to Exhibits 1 through 7, relating to subdivisions, the given number to be furnished by San Gabriel from their records.

I understand counsel will consider that.

Mr. Constable: Your Honor, without being committed, of course, as I understand Mr. Shearer's offer, it is really in effect an offer to stipulate that we will stipulate. Well, now, we will do everything we can, and it is my opinion that this [82] thing should be a matter of fact, and I think we

(Testimony of M. E. Moseley.)

can agree on it. We will certainly cooperate with him and do everything we can to accommodate him.

The Court: All right.

Cross Examination

Q. (By Mr. Constable): Mr. Moseley, the water contracts which your company has with subdividers, wherein certain refunds or advances are provided, have for their purpose, do they not, the fact that the water companies by these contracts are then providing installations with funds provided by the contractor; isn't that correct? A. Yes.

Mr. Shearer: Will you read the question and answer, please?

(Record read.)

Q. (By Mr. Constable): Have you brought with you your 241 ledger for job No. 297-W?

A. Yes, sir.

Mr. Constable: Will you mark this exhibit?

The Clerk: X.

(Respondent's Exhibit X was marked for identification.)

Q. (By Mr. Constable): I will show you what is marked for identification as [83] Exhibit X. Counsel in this case will agree that Exhibit X is a transcript of your job 297-W. This is a contract, is it not, or the job number for a contract between San Gabriel Water Company with Albert Gersten and Myron P. Beck? A. That is correct.

Q. And what is the date of deposit, approximately?

(Testimony of M. E. Moseley.)

A. Approximately September 5, 1946 was the date of the contract. The deposit should have been reasonably close to that.

Mr. Shearer: May I move to strike for purposes of making an objection?

The Court: Yes.

Mr. Shearer: I object to this question on the ground it is immaterial to the issues here involved; for the Court's understanding, this does not relate to any of the specific transactions in issue, here in issue.

Mr. Constable: I might say, your Honor, if I could describe through the witness this contract, its effect, I will then offer it and counsel can object to its admission.

Mr. Shearer: If this is purely for description purposes, I will withdraw my objection. I did not want to be in a position of waiting too long to object.

The Court: All right.

Q. (By Mr. Constable): This contract, or this job No. 297-W, indicates that [84] the contract was made in September of '46, and that is similar in many respects, most respects, to Exhibits 1 through 7; that it expired in September of 1956, but that by October '54 it had paid out completely; is that correct?

Mr. Shearer: Just a moment. Now, I object to that question, and if counsel proposes to put this into evidence—he is first reading it into evidence and then he is going to put the exhibit in.

(Testimony of M. E. Moseley.)

so I am afraid I am going to have to object to the evidence that he is now seeking to elicit, which is simply a reading of this proposed exhibit.

Mr. Constable: All right, your Honor, I will withdraw my question. I can go about it another way.

The Court: All right.

Mr. Constable: At this time I am going to offer into evidence Exhibit X, your Honor. Now, this particular exhibit, counsel has stipulated with me that it is a true copy of job No. 297-W on the books of San Gabriel Valley Water. The document speaks for itself in many respects. It is a contract with the water company between Gersten. It is in prior years.

I might state that the amounts here involved or the contract represented by this document have no bearing on the computation of the deficiencies involved.

The Court: What is the purpose?

Mr. Constable: The purpose, your Honor, is to show that here we have a prior contract made by Albert Gersten, which [85] was made in September of '46, and by the end of 1950 had paid out in refunds 10,000 of the original 18,000. Now, the purpose is to show that by 1950 Mr. Gersten and Mr. Beck were aware that these particular contracts were paying out.

The Court: Might show that they could be aware that this one was.

Mr. Constable: We further have a stipulation,

(Testimony of M. E. Moseley.)

your Honor, from Mr. Shearer that this particular job number, this refers to a tract which is in the neighboring area of the other tracts in issue.

The Court: All right.

Mr. Shearer: I think you are incorrectly stating it—I may be wrong, there is so much here—but I think that is an incorrect statement of the stipulation.

Mr. Constable: Now, your Honor, let me give you the background on this. Of course, I at first offered to stipulate——

Mr. Shearer: Are you saying that it is part of the written stipulation or that I undertook to stipulate?

Mr. Constable: You stated that this was a true document. You stipulated that if it was material then you would stipulate that it was in the area of the tracts in issue.

Mr. Shearer: That is correct.

The Court: All right.

Mr. Shearer: I was confused. I thought that counsel was——

Mr. Constable: That is my offer. [86]

The Court: All right.

Have you stated your objection?

Mr. Shearer: I object on the grounds that this has no bearing, doesn't tend to prove or disprove any of the issues here involved.

The Court: The objection is overruled. It will be marked in evidence.

The Clerk: Exhibit X received.

(Testimony of M. E. Moseley.)

(Respondent's Exhibit X was received in evidence.)

Q. (By Mr. Constable): Mr. Moseley, referring to Exhibit X, are you able to determine approximately, as of December, 1950, whether that particular contract will pay out?

A. As of December, 1950?

Q. Yes. A. No.

Q. Mr. Moseley, from looking at the refunds which are coming in by year on the tract involved, or the refunds being paid per each year, isn't it possible to arrive at some sort of conclusion as to whether by the expiration date this contract will pay out?

A. If conditions stay as they were or are at the moment.

Q. At 1950? [87]

A. Yes, if conditions should stay that way, if the occupancy stays the same.

Q. If the occupancy stays the same. What other conditions must stay the same, Mr. Moseley?

A. Oh, I related things that would vary; refunds, weather, condition of properties, economic conditions certainly.

Q. Now, thinking back to, oh, during the period 1949 to 1950, barring the possibilities of depressions and floods and earthquakes and droughts, and ignoring the occupancy question, isn't it a conservative estimate to say that at least 70 per cent of the refunds will be made on the contracts which San Gabriel Water Company has with subdividers?

(Testimony of M. E. Moseley.)

Mr. Shearer: Will you read that question, please?

(Question read.)

Q. (By Mr. Constable): You may answer.

A. When I heard the question read, the lady said 70 per cent of the contracts which the water company has with subdividers. I don't know that that would be——

Mr. Constable: I believe I said, "Is it not a conservative estimate that 70 per cent of the refunds would be made under the contracts which San Gabriel had with its builders?"

The Witness: I believe it would be.

Mr. Constable: That is all, your Honor. [88]

Redirect Examination

Q. (By Mr. Shearer): Mr. Moseley, is your 70 per cent an average figure?

A. No. Oh, I beg your pardon.

Q. The 70 per cent answer you gave to the last question, are you giving that as an average figure?

A. That would be what it would amount to, I'd say.

Q. Do you believe that there will be some which will pay off less than 70 per cent?

A. You mean at this time or in 1950?

Q. Speaking as of 1950, with respect to the contract you then had, and having in mind the various factors you took into account——

A. Yes, some would pay off much less than 70 per cent.

(Testimony of M. E. Moseley.)

Q. Some would pay off at more than 70 per cent? A. Yes, sir.

Mr. Constable: I would object. I don't mind leading, but I hate to have to be bothered with it.

Mr. Shearer: I refrained—and perhaps that was where I made my error—from raising any question of whether counsel's questions were cross examination or whether counsel simply took over the witness and was using him as his own expert.

Mr. Constable: May I respond?

Mr. Shearer: I am directing my attention to new matters that counsel has raised, and I take it that in that respect I have some more latitude.

The Court: I think that the questions that were asked were cross; in the proper range of cross examination.

Q. (By Mr. Shearer): During the year 1950, Mr. Moseley, was it known the freeway was to go through or near the area in which San Gabriel serves?

A. Certain areas, yes; not this particular area.

Q. Well, when you say "this particular area," you mean Whittier Downs?

A. The vicinity of the subdivisions for which we made contracts with Mr. Gersten and his associates.

Q. Have you brought with you a map which counsel subpoenaed, relating to this area?

A. Yes, sir.

Mr. Shearer: Will you mark this for identification, please, Mr. Clerk?

(Testimony of M. E. Moseley.)

Your Honor is correct in referring to 8, but my recollection is that that was an exhibit offered by respondent; in fact, to which I had made unsuccessful——

The Court: Just hold the number, Mr. Clerk.

Mr. Constable: That is not correct, your Honor. Exhibit 8 was the copy of job 603, which is that Whittier contract made—we stipulated that that one may go into evidence.

Mr. Shearer: I stipulated as to form, and I stipulated with him just as I stipulated with respect to the job number— [90] that is in paragraph 7 and 8—so I am not questioning the propriety or the form. I am saying that, far from offering it, I objected to it, and although its prototypes were included in the stipulation at the request of counsel—and I do stipulate and do not withdraw my stipulation with respect to the accuracy of the facts——

The Court: In other words, what you are trying to say, you don't want it numbered as an exhibit of petitioners.

Mr. Shearer: I certainly do not, because I wish my objection accorded to it.

Mr. Constable: I will certainly take it, your Honor.

The Court: Well, it is immaterial to the Court.

Mr. Constable: Does the Court wish to change the marking on it.

The Court: If petitioners' counsel is correct—I wondered about it at the time, that no mention

(Testimony of M. E. Moseley.)

was made of the fact, though I made no vocal note of it. But if it is, as counsel states, not an exhibit of petitioners, it should be marked as an exhibit of respondent's.

Mr. Constable: I might say, your Honor, that it was my impression that the stipulation covering what is shown as Exhibit 8, the objections to that exhibit were much the same as the objections to all of the similar job transcripts shown in the stipulation, is that correct?

Mr. Shearer: That is correct, that we offered as part of [91] the stipulation, and not as an exhibit.

The Court: Let me see it, please.

(Document handed to the Court.)

The Court: What is the last exhibit for the respondent?

The Clerk: X.

The Court: It would be a rather strange-appearing thing for the record to have an exhibit marked in as an exhibit of the party who raised an objection, even though the objection was as to materiality and it was overruled; and since, as I understand, this exhibit is in substance comparable to those which are a part of the stipulation, and to which the petitioners' counsel did object, it would appear to me that it would be appropriate for this to be marked as respondent's exhibit because it would appear to me that the respondent is really the one that was offering it. So we will let the record show that the exhibit heretofore marked as

(Testimony of M. E. Moseley.)

8 will become Exhibit Y, unless I hear something to the contrary as to why that should not be done.

Mr. Constable: It is satisfactory.

The Court: The last exhibit, then, that we have of the petitioner is Exhibit 7, is that right?

Mr. Shearer: Yes, your Honor.

(Respondent's Exhibit Y was marked for identification and received in evidence.) [92]

The Court: All right. Now, then, let this next one be Exhibit 8, marked for identification, which is a map, as I understand, produced by this witness.

The Clerk: Yes, your Honor, Exhibit 8 for identification.

The Clerk: Identified as Petitioners' Exhibit 8.

(Petitioners' Exhibit Number 8 was marked for identification.)

Q. (By Mr. Shearer): Does Exhibit 8 contain a property which San Gabriel services under its franchise?

A. Yes, under one of its franchises and certificates.

The Court: What is Exhibit 8? Whose is it; who prepared it; what was the occasion of preparing it? What is it?

The Witness: This was prepared—this print was prepared at the request of Mr. Constable, who asked me if I would bring it to court today.

The Court: And it was prepared by whom?

The Witness: It is a copy of a tracing which is in our office that is regularly used in our business,

(Testimony of M. E. Moseley.)

and it is a direct print. It is a map drawn to a scale of 600 feet to the inch, and on it are depicted water pipe lines, pumping plants of San Gabriel Valley Water Company, tract numbers, and streets, and an indication of the political subdivision of the City of Whittier, and the San Gabriel River.

The Court: All right, go ahead. [93]

Q. (By Mr. Shearer): Are all of the tracts covered by Petitioners' Exhibits 1 through 7, inclusive, depicted on Exhibit 8 for identification?

A. Sir, I haven't seen the exhibits.

The Court: I have been wondering about that, asking this witness questions about 1 through 7, as to whether he knew what you were talking about.

Mr. Shearer: I think he misunderstands what it is, because he has seen it earlier this morning.

The Court: Maybe he has, but there isn't anything in this hearing up to now to indicate that he would be aware of what you were asking him.

Q. (By Mr. Shearer): You examined these this morning, did you not, Mr. Moseley?

A. Yes, sir. I did not take a look at the exhibit numbers that are marked on them.

I believe so. Just let me check a moment to be certain.

The Witness: May I be permitted to circle the tract number on the map as I check them?

The Court: Well, that depends on whether counsel wants it or whether it is desirable or what; I don't know.

(Testimony of M. E. Moseley.)

Mr. Shearer: Yes, it is agreeable.

Mr. Constable: I have no objection. [94]

The Court: All right.

A. The first tract number is 15062; that is Exhibit 1, and that tract is here (indicating).

The next tract is 11838. That tract is on this map.

The next one is 15741, and that is on this map.

Tract 14001 is on this map, and tract 11970 is on it, and tract 15650 is on it. So they are all on this map.

Q. (By Mr. Shearer): Is the tract referred to on respondent's Exhibit X, which I believe is tract 13977 on the map?

A. That tract is on this map. And I have circled it, as I did the others.

Q. Now, have you had any word about the freeway touching any part of the property——

I'm sorry.

Mr. Shearer: I don't know whether I offered this yet or not.

The Court: It has been marked for identification.

Mr. Shearer: I will offer it in evidence.

The Court: Any objection?

Mr. Constable: No objection.

The Court: It will be received and marked in evidence.

The Clerk: Exhibit 8 in evidence.

(Petitioners' Exhibit Number 8 was received in evidence.) [95]

(Testimony of M. E. Moseley.)

Q. (By Mr. Shearer): Directing your attention to Exhibit 8, are you aware of a proposed freeway going through any portion of Exhibit 8?

A. Yes.

Q. Of the property depicted on Exhibit 8. And do the plans for that proposed freeway touch on any of the tracts which you have marked?

A. Yes. The plans for that freeway go through tract 15650.

Q. Will that have a substantial bearing upon the occupancy factor, assuming the freeway is completed in accordance with the plans?

A. Well, the houses in the road of the freeway would be removed, no longer buy water.

Q. Approximately how many houses would be involved, if you know?

A. I don't know, sir.

Q. Now, have you brought with you the ledger sheet relating to job No. 665-W? A. Yes, sir.

Q. Is the ledger sheet entitled "Job No. 665" a similar type of ledger sheet to that of Respondent's Exhibit X, which relates to job No. 297-W?

A. Yes, sir.

Q. Does job No. 665-W, which covers tract 15377, is [96] that in the same general area as the tracts which were depicted on the map which you marked?

A. My recollection is that all of the tracts with Mr. Gersten are on this map; there are many tracts on here. I can't find it at the moment.

The Court: Are the job numbers on the map?

(Testimony of M. E. Moseley.)

The Witness: No, sir. The job numbers are directly related to the tract. The tract numbers are on the map. Here it is.

The Court: I was wondering, when I start looking at that map, I can tell that you have circled certain areas, but will I know from that which one of those contracts it relates to, or which one of those accounts it relates to.

Mr. Shearer: The exhibits have the job number and the tract number.

The Court: That is what I am asking. Is there any common identification as between the exhibits, those job numbers and the tracts as shown on the map, so that I can identify them when I look at the map?

The Witness: Each of the exhibits has the tract number to which it relates. It does not have the job number.

The Court: Does the tract number, then, appear in places where you have circled?

The Witness: It does.

The Court: The same tract number that is on the other [97] exhibit?

The Witness: Yes, sir.

The Court: All right, that is all I was asking.

The Witness: I have located 15377, if I haven't lost it again. Here it is.

Mr. Shearer: I will offer Petitioners' next in order, the ledger sheet containing job No. 665-W, and since I don't have a copy, I will ask for leave to substitute a photostatic copy, your Honor.

(Testimony of M. E. Moseley.)

The Court: Any objection?

Mr. Constable: This is Exhibit 9, is that correct?

Mr. Shearer: Yes.

The Court: It will be the next exhibit. This is the ledger sheet.

Mr. Constable: Your Honor, I question the materiality of this particular document. It is a contract made with, I believe, somebody named Crown Land Company, and it appears that the contract was made in August of 1950. I will object to it on the grounds of materiality.

The Court: The objection is overruled.

(Petitioners' Exhibit Number 9 was marked for identification and received in evidence.)

Q. (By Mr. Shearer): You stated, I believe, that these contracts had for [98] their purpose the fact that the subdivider, by these contracts, paid for the installations?

Mr. Constable: That assumes a fact not in evidence.

The Court: Let him finish the question.

Q. (By Mr. Shearer): Did you mean by that answer that that was the contractor's purpose or your purpose?

Mr. Constable: Objected to as assuming a fact not in evidence. I think that the testimony was on cross that the subdivider financed, and not paid. I think the question assumes that the subdivider is paying for installations, and the evidence is that

(Testimony of M. E. Moseley.)

the subdivider merely financed it, that is, provided the water company with financing.

Mr. Shearer: This ought to be easy to find because, as I recall, it was the first question on cross examination, and I would like the reporter to find that, because my recollection and notes indicate that the question related to it, related to the payment and the financing.

The Court: All right. I think we might as well have it found.

Reporter (Reading): "Question: Mr. Moseley, the water contracts which your company has with subdividers, wherein certain refunds or advances are provided, have for their purpose, do they not, the fact that the water companies by these contracts are then providing installations with [99] funds provided by the contractor; isn't that correct?"

The Court: You withdraw your question?

Mr. Shearer: Yes.

Q. (By Mr. Shearer): You have testified, then, that the purpose was to have the funds provided by the contractors. Whose purpose was that, Mr. Moseley?

A. That's the subdivider, the contractor's purpose, if I understand you correctly.

The Court: I think that one of the difficulties with all of this examination up to now is that there is too much of a tendency to try and inject conclusions, resulting conclusions into questions that are asked of witnesses, rather than to ask the facts.

(Testimony of M. E. Moseley.)

All right, the witness has answered the question. Go ahead.

Mr. Shearer: No further questions.

The Court: What is that?

Mr. Shearer: No further questions.

Recross Examination

Q. (By Mr. Constable): Referring to Exhibit 9—do you have that before you? A. Yes, sir.

Q. Does that job refer to a tract of residential [100] property?

A. Principally residential property. As I recall, there is one business lot in it, and the balance is residential.

Q. You testified in connection with Exhibit 8, the tract map, concerning a freeway running through the map? A. Yes, sir.

Q. When did the plans for that freeway become final?

A. The State of California has adopted a route; plans are not final yet.

The Court: What is the implication between adopting the route as against the plans being final? What do you mean?

The Witness: I have read that statement in the paper, and it has been relayed to me by State employees that have visited me in connection with it; and I presume it is a declaration of intention as to a close approximation of a location of a freeway or highway. That's what I believe it to be.

(Testimony of M. E. Moseley.)

The Court: But you don't understand it is yet final?

The Witness: I know that the plans are not drawn at all.

The Court: I see.

Mr. Constable: That is all I have, your Honor.

The Court: I have a question or two.

Examination

Q. (By The Court): You at one point were answering a question as to factors bearing upon use of water in a subdivision. You [101] mentioned the size of the lot, vegetation, pride of ownership, as I recall? A. Yes, sir.

Q. Now, those things have to do, at least they would mean to me, factors that are outside the house. A. Yes, sir.

Q. What about the facilities and the range of facilities for use of water in a house? Do you normally regard that as being something as indicative of probable use of water?

A. We do, sir, and for this reason: The use of water all over the United States is growing constantly. We have many new devices that use water; automatic washing machines, garbage disposals use a great deal of water. But out here in California, I think our largest use is for irrigation purposes. We found ourselves in a position last year of running into the seventh month before we were out of the red.

The Court: I don't know what you mean.

(Testimony of M. E. Moseley.)

A. I mean the water company, the sales were not sufficient to cover its expenditures, its expenses for the first six months of last year. So that that is reflected by smaller sales in the winter than in the summer. And the water use inside a house is not particularly connected with the season.

Q. You wouldn't say that it doesn't have some relation to variation of seasons, would you?

A. It did, but not as much as the irrigation.

Q. Well, now, you say that irrigation is an important factor, after making the statement that the use of water through house facilities is a factor and, I judge, important throughout the United States. You don't mean by that that it is not important here, do you, like washing machines, showers, baths, dish washers, disposals, and the normal use in the house?

A. I still say that——

Q. I am just asking you, is that a substantial factor?

A. It doesn't compare with irrigation. It is substantial.

Q. All right. Now, then, have you in your experience made any study of that—and you, by reason of that experience, as manager of the water company, have some knowledge of the fact of the ratio as between the outside and the house use of water?

A. May I refer to some things I have with me that I may be able to answer that better?

Q. I don't know what you have in mind.

A. I have in mind statistical information that

(Testimony of M. E. Moseley.)

we keep for the purpose of knowing what our peak loads are and how much water we are delivering per customer and how much water is going to be required to meet a summer's load, and so we keep records of our pumping.

Q. Your water for a house and lot all goes through the same meter, doesn't it?

A. Yes, sir. [103]

Q. So those different uses you would arrive at by some other studies other than the meter reading, namely, your season — that when they were using water outside or things of that kind; is that what you are talking about?

A. When it becomes necessary to use water outside, we sell a great deal more than we do in the winter time, much more.

Q. Now, in functioning as manager of a water company, do you, as such manager, have any occasion to note a rise or fall in the areas served by you of occupancy of houses? A. Yes.

Q. That would have a very direct bearing from your month-to-month use of water, wouldn't it?

A. That would.

Q. If it was an area that was fully occupied or if it wasn't occupied? A. That's true.

Q. In the period from, say, '47 through '50, and as manager of the water company in the course of your duties, noting such things, did you note any signs of extensive unoccupancy or vacant houses in the area served by your company?

A. No, sir.

(Testimony of M. E. Moseley.)

Q. Would you say that there was comparatively full occupancy or a major portion of occupancy, or what would you say about it?

A. I would say there was a comparatively full occupancy. [104]

Q. Has that varied since?

A. That condition——

Q. Has it continued or has it changed?

A. That condition still prevails throughout Whittier, so-called Whittier area. I guess I will have to explain that.

Q. Is that the area that you were marking on the map?

A. Yes, sir. That is a portion of our Whittier district. That doesn't apply to our Fontana district.

Q. Are any of these areas that are covered by those contracts in your Fontana district?

A. No, they are not.

The Court: All right. I have asked the witness some questions. In case my questions have suggested questions counsel desire to ask, you may ask them.

Mr. Shearer: I have one question in connection with that.

Further Redirect Examination

Q. (By Mr. Shearer): You stated on examination-in-chief that the income of the occupant had a bearing on the use of water, did you not?

A. Yes, sir.

(Testimony of M. E. Moseley.)

Q. And his Honor referred to the inside use of various appliances.

In the normal course of events, will a home with two bathrooms and more appliances use more water than a home with one bathroom and less appliances? [105] A. Yes.

Mr. Shearer: No further questions.

Further Recross Examination

Q. (By Mr. Constable): How far is Fontana from Whittier? A. It is 35 miles.

Q. How far? A. Thirty-five miles.

Mr. Constable: That is all.

The Court: Would there be any relationship in, say, the pride of ownership in a two-bathroom house as against a pride of ownership in a one-bathroom house?

The Witness: No, I don't think that depends on the number of bathrooms.

The Court: Do you think that would have any bearing, likewise, as to outside use of water?

The Witness: No, I guess a two-bathroom house could go on any size lot. It wouldn't have any bearing.

The Court: All right. Any more questions?

Mr. Constable: That is all.

The Court: You are excused.

(Witness excused.)

(Discussion off the record.)

Mr. Constable: May that map be left with the Court?

Is that a copy? [106]

Mr. Shearer: Yes, I prepared a copy and it may be left in evidence. I don't wish it.

Mr. Constable: I subpoenaed it. I wanted to make sure.

The Court: All right.

Mr. Shearer: Call Mr. Garnier.

CAMILLE A. GARNIER

was called as a witness by and on behalf of the petitioners, and, having been first duly sworn, was examined and testified as follows:

The Clerk: Please state your name and address.

The Witness: Camille A. Garnier, 16340 Maple Grove Avenue, Puente.

Direct Examination

Q. (By Mr. Shearer): Mr. Garnier, state your occupation.

A. I am president and general manager of Suburban Water Systems.

Q. Are you also engaged in the subdivision business?

A. Oh, yes, we build 30 or 40 houses a year is all.

Q. How long have you been president and general manager of Suburban or its predecessors?

A. I have been president and general manager of Suburban Water Systems and its predecessor corporations since 1944.

Q. Is Suburban a private company similar to that of San Gabriel? [107] A. Yes.

(Testimony of Camille A. Garnier.)

Q. You are subject to the regulatory supervision of the California Public Utilities Commission?

A. That is correct.

Q. I show you Exhibit 1 and direct your attention to the first and second paragraphs thereof. Will you examine them, please? A. Yes.

Q. Now, are you familiar with contracts of the nature of Petitioners' Exhibit 1? A. Yes.

Q. Have you acquired that familiarity in connection with your work for Suburban?

A. As a public utility, Suburban, San Gabriel, and practically all the rest of the public utilities in California operate under the same rules and regulations; as a result of the rules, the contracts are similar.

Q. And you are in charge of the negotiation of similar contracts with subdividers in the Los Angeles area? A. Yes.

Q. You heard Mr. Moseley's testimony, did you?

A. Yes, sir.

Q. Is it true that you are concerned with the cost of the installation of the water pipe lines?

The Court: I think that you better develop what you want [108] this witness to testify without—I don't want to have to turn back and read the testimony of the other witness. If you want to know something from this witness about his work and his experience and how he goes about it, suppose you ask him.

Mr. Shearer: Yes, your Honor.

The Court: That is a very general question, and

(Testimony of Camille A. Garnier.)

I would have to go back and possibly read the other witness' testimony when I get down to that part of the transcript.

Q. (By Mr. Shearer): Mr. Garnier, how do you arrive at the amount which the subdivider is required to pay in connection with any water facility contract?

A. Our company requires a subdivider to deposit with it a subdivision plat map of its installation. The company's engineering department makes a layout of the water estimates required to properly serve the residential, commercial, and other types of customers that will be incidental to that development. An analysis is then made of the cost to make such an installation, and that estimate is given to the subdivider and the subdivider makes a deposit of that amount of money. Upon the receipt of the deposit by the company of the subdivider's money, the installation is made. In exchange for the deposit, the subdivider is given a refund agreement.

Q. The amount which the customer pays is the amount determined by you or Suburban to be the cost of the installation, [109] is that correct?

Mr. Constable: Your Honor, I would rather hear the witness testify.

The Court: I think he just testified to that effect.

Well, I think he has testified probably better than you are there, so——

Mr. Shearer: I was simply trying to save time in transition. I can go about it the long way.

(Testimony of Camille A. Garnier.)

The Court: All right, let's go about it in an orderly way, because this witness gave you a very clear and definite answer there. If you will just ask him the question, I am convinced that he will answer it.

I sustained the objection.

Q. (By Mr. Shearer): Is the amount of payment based solely on cost of installation?

A. Yes. The amount of payment is based upon the cost of the installation. However, the cost to the subdivider per lot will vary very widely, depending upon the location of the subdivision, in relation to the balance of the water system, the size or the frontage of the lots involved, the necessary line sizes to be paid by the water company, and in general it will result in a deposit by the developer of from $90 to $230 per lot, and I am taking that as an average of, oh, the last million dollars of these deposits received by our company. [110]

Q. May the nature of the soil affect the cost of the installation?

A. Soil type requiring different types of material to be used is one of the many factors involved in arriving at a cost per lot in any subdivision.

Q. Now, does the cost of the water pipe installation necessarily involve a greater use of water—strike that.

Would the fact that the cost of a water pipe installation was increased by the distance from the water company's nearest facility to the subdivision result in a greater use of water in that subdivision?

(Testimony of Camille A. Garnier.)

The Court: Now, let's have the reading of that, so that we can all listen to that.

(Question read.)

The Court: That is a very hard question to follow. I believe you can do better than that.

The Witness: I think I know what he is getting at.

The Court: I can guess at it myself, but I don't like to have to guess at it.

Q. (By Mr. Shearer): Has it been your experience that the ultimate occupants of a subdivision use more water because that subdivision was a substantial distance from your nearest facility at the time of the installation of the water mains in that subdivision?

A. The answer to your question, the cost of installing a [111] subdivision or the cost to a subdivider of making the necessary main installations to serve a particular user of water within a subdivision has little relationship to the distance of that subdivision to the company's nearest facility. However, there are about 15 factors that very considerably influence the amount of water used by the main, which in turn influences the amount of refund received by the subdivider.

Q. What factors do affect the amount of water which may be used in a subdivision during any given ten-year period from the completion of the water installation of a new subdivision until the end of that ten years?

A. The factors that are to some degree influenc-

(Testimony of Camille A. Garnier.)

ing the amount of water that will be used by a consumer in any specific subdivision are as follows:

1. The location of the subdivision and the type of land on which it is located. First, the type of soil makes a considerable difference in the amount of water used, because if it is sandy in nature, as many areas are in Southern California, the amount of water used outside of the house in the averages of the Suburban Water System, which serves areas adjacent to those about which Mr. Moseley testified, there is approximately seven to eight hundred cubic foot of an average monthly bill used within the residence, with an average for 1954 in our company of over 23,000 services of about 2,180 cubic feet used as an average for the average customer for the year, which [112] means that the difference between 800 cubic feet and 2,100 or 2,200 cubic foot is used outside of the house. So the type of soil, if it is sandy in nature, means the lawn has to be irrigated every day instead of once or twice a week, as an example.

The next factor is, if the subdivider plans lawns and shrubs at the time of the construction of the house, and that is a part of the house at the time it is purchased by the buyer, it means that the first five or six months of occupancy, there is a great deal more water used than if it is dependent upon the installation of this lawn and shrubbery by the new tenant and owner, who is busy getting installed in the house.

The next matter of temperature, for the year, the

(Testimony of Camille A. Garnier.)

amount of sunshine and the relation of rainfall. We have been normalizing our company's water use as a result of temperature, and find a difference as high as 28 percent in gross water use from a low user and a high user.

The Court: That is your margin of variation?

The Witness: Yes, sir.

The Court: Found from your study?

The Witness: From our study. We have just completed the study for rate purposes. Next, the rates of the water company are an influencing factor in water use. Where water is sold at a flat rate with no extra charge for waste, a lot of waste takes place. If the rates are low, many times the water use will be 40 to 60 percent greater than where rates are higher. [113]

The continued occupancy of the house is an important factor, and that varies as a result of people moving in and out, if they are tenants, or if they are taking prolonged vacations where the house is left vacant. Those are principally the factors that affect water use.

Q. (By Mr. Shearer): Mr. Garnier, in general, in the first year of a typical water pipe installation such as Petitioners' Exhibit No. 1—strike that.

Is the use of water during the period of construction of a home substantially less than the use after occupancy by the ultimate purchaser?

A. The use of water during the first year of the installation of a subdivision—and I am predicating this answer on one type of subdivision, which is a

(Testimony of Camille A. Garnier.)

house-building subdivision—however, a third of the subdivisions installed are not house-building subdivisions, and in some of those subdivisions the occupancy, full occupancy is not arrived at for from five to seven years, which is a very deciding and influencing factor.

One of the big factors is the speed at which the subdivider is able to construct his house, and that speed of construction will vary from four months to two years, depending upon a group of three factors. 1, availability of labor; 2, availability of material and material strikes, in which I have seen subdivisions late four weeks to two and a half months; and [114] also finance; finance because of terms of payment. The terms of payment for the house will in turn cause have wide differences in the speed of sales.

The Court: You are talking about now financing through a purchaser, individual purchaser of a house?

The Witness: Yes, sir. The type of finance, whether it be no down payment or whether it is necessary that the buyer pays a thousand or two or three thousand dollars down. In fact, I know of my own knowledge of a tract that Mr. Gersten, who is here before this Court, took him almost two years to sell all the houses in it. Therefore, the speed of sale and the speed of closing the transaction after the sale, which is the result of trying to clear up the red tape of Governmental agencies involved—I personally have had experience where the Veter-

(Testimony of Camille A. Garnier.)

ans Administration has taken six months to conclude a sale through their office after a bona fide sale was made and the down payment was received in the sales office.

The Court: Now, just a moment, because I think that you are getting beyond the question. The question was directed to different uses of water during the period of construction; at least——

The Witness: Yes, I did get beyond it. I should say during construction and to the time of the occupancy of a buyer, which from that time on there is continual occupancy and continual water use. [115]

The Court: And that is greater or less than during construction?

The Witness: During a construction period, the use of water—our company makes a charge of $2.50 for all of the water that will be used during the entire construction period and up to the time of the occupancy of the person who is going to live in that house; and the minimum usually—I mean I am taking out of seven rates—is from $1.75 to $2.50 per month. Therefore, the ratio of water return or revenue, which in turn influences a refund to the subdivider, is hardly nothing during the construction period.

The Court: All right. I think that is where the question was.

The Witness: Thank you for your assistance.

Q. (By Mr. Shearer): Mr. Garnier, speaking as of the commencement of the installation of the water pipe lines, can you predict at that time how

(Testimony of Camille A. Garnier.)

much, if any, of the water pipe payments may be refunded?

A. No, sir, it is an impossibility.

Mr. Shearer: No further questions.

Cross Examination

Q. (By Mr. Constable): Have you ever personally bought one of these contracts?

A. Yes, sir. [116]

Q. How many have you bought?

Mr. Shearer: Just a moment, please. Now, the last time I ran into this difficulty—I am going to object on the ground that this is improper cross examination. I may say, for convenience, I have no objection if respondent wishes to offer this as his evidence, so that I may——

The Court: You are objecting on the grounds that this is improper cross?

Mr. Shearer: Yes.

The Court: The objection is overruled.

If it later develops that it appears that it is, you may object again, but it isn't up to this point.

You may proceed.

Q. (By Mr. Constable): Are you familiar with the area shown on Exhibit 8?

A. Could I see Exhibit 8?

Yes, sir.

Q. This is generally sandy soil, is it not?

A. Well, I would say more loamy, sandy, loamy soil. It isn't as sandy as some of the other areas.

(Testimony of Camille A. Garnier.)

Some areas of it is heavy soil, in fact, in the north part.

Q. It is true, isn't it, that in 1949, 1950, there is, as affecting your company, a dollar and twenty-five cents minimum payment by water users to be made to your company for the use of water? [117]

A. No, sir, not of my knowledge.

Q. Are you familiar with the PUC regulations with regard to minimum payments?

A. Very familiar.

Q. Does that vary from company to company?

A. Yes, sir, it varies within companies. That is another large factor in determining a refund, because of the rate schedules within a company. We have seven different rate schedules going from $1.75 to $7.00 as a minimum to a customer within our company.

Q. Referring to the area shown on Exhibit 8, would you say——

The Court: Let him see it.

The Witness: Isn't that the one you just showed me?

Mr. Constable: Yes, that is the map.

Q. (By Mr. Constable): Referring, Mr. Garnier, to the area shown on Exhibit 8——

A. Are you speaking of the area within the boundaries of the San Gabriel Water Company?

Q. That is correct. A. All right.

Q. It is true, isn't it, that a minimum rate of $1.25 would be exceeded by most of the home users

(Testimony of Camille A. Garnier.)

in the tracts shown as 15650 and other tracts circled in pencil? [118]

A. I am sorry, but I don't believe I could answer the question, for the reason that it would take an analysis of the rate structure and the rate and the use of water by the average customer in that area, and I do not have those figures or have never examined them.

Q. I think you testified that you could not predict the amount of refunds to be obtained on a water deposit contract?

A. Yes, sir. It is very difficult to predict it with any certainty.

Q. But it can be predicted?

A. Yes, within bounds, yes, sir.

Q. And on the basis of that prediction, you bought some contracts?

A. I bought a contract.

Q. A contract? A. Yes, sir.

Mr. Constable: That is all, your Honor.

Redirect Examination

Q. (By Mr. Shearer): Did you buy that contract personally? A. Yes, sir.

Q. Was the subdivision to which it related fully completed when you bought it?

A. Well, the houses had been installed and fully occupied for a period of about four years. [119]

Q. Where was this property?

A. West Covina.

Q. How much did you pay for that contract?

(Testimony of Camille A. Garnier.)

A. I think we paid about $8,400 for a $6,800 contract.

Mr. Shearer: No further questions.

Recross Examination

Q. (By Mr. Constable): Mr. Garnier, you have purchased contracts or a contract, you say, personally; then you said "we." Now, whom were you referring to?

A. Could you repeat the question?

(Question read.)

A. Well, I am speaking for my sister and myself, who is in business with me.

Q. Now, Mr. Garnier, in addition to purchasing some of these contracts personally, you have, have you not, through companies in which you have a financial interest purchased some of these similar contracts?

Mr. Shearer: Again I am going to object on the ground that this is improper cross examination.

The Court: The objection is overruled.

The Witness: Would you repeat the question?

(Question read.)

A. Yes.

Mr. Constable: That is all, your Honor. [120]

Mr. Shearer: I would like to examine further on the new matter raised by counsel.

The Court: Well, I don't know whether there is any new matter that has been raised, but if you have some questions, you may ask because he is your witness.

(Testimony of Camille A. Garnier.)

Further Redirect Examination

Q. (By Mr. Shearer): What companies purchased these contracts?

A. Well, it is a little difficult to answer that question so that it would be properly interpreted. It would be necessary for me to make a statement prior to that, if that is agreeable, because the purchase of the contract within our company, which has been very limited, is for a purpose—not a basis—utterly different than was ever available to Mr. Gersten.

Mr. Constable: I object. I move that this be stricken.

The Court: Well, I think if you can answer the question, then if there is any explanation called for, why, it may be asked.

Let's get back to the question.

(Question read.)

The Court: Let the record show that he is asking what company.

A. I think Garnier Construction Company purchased a contract. [121]

Q. That is in addition to the contract to which you referred when you spoke of a purchase by yourself and your sister? A. That is correct.

Q. Now, when did Garnier Construction Company purchase this contract?

A. I wouldn't know. It would be in the last two years probably.

Mr. Shearer: No further questions.

(Testimony of Camille A. Garnier.)

Further Recross Examination

Q. (By Mr. Constable): You know the company named California-Pacific Finance, do you not? A. Yes, sir.

Q. You also know a Mr. Brittain?

A. Harry Brittain?

Q. Yes.

A. What is his address? I know two or three Brittains. That's the reason I ask.

Q. Harry L. Brittain.

A. What location?

Q. Gunn and Telegraph.

A. Yes, sir, I know the gentleman.

Q. Yes. Now, isn't it true that you encouraged in this deal, in a deal with these two parties——

A. Two parties? Which is the other party?

Q. California-Pacific Finance, whereby you, in effect, traded preferred stock of your company for the builder's contract?

Mr. Shearer: May I ask the purpose for which this question is directed? Otherwise, I object to it on the ground of its immateriality.

The Court: Well, I assume it is a part of the cross, which is directed, as the other was, to testing the soundness of the first categorical answer, that you couldn't estimate that there would be any refund.

Mr. Shearer: Your Honor, that question related to a specific kind and specific time, and the fact that many years later—several years later this witness may or may not have been involved or not in-

(Testimony of Camille A. Garnier.)

volved in the purchase, I submit, is neither proper cross examination nor material to the issues here involved.

The Court: The objection is overruled.

Read the question.

(Question read.)

The Court: The question about being able to determine the refunds, so to speak, on the basis of water use—your question was not based on any particular time or as of a particular time. It was a general question. So for that reason, among others, this is proper cross and—may not develop [123] to where it amounts to anything, I don't know about that, but we will see, and if it does or it doesn't, the Court will determine it when it starts considering the evidence and finding the facts.

The Witness: Would it be fair to ask for a restatement of that question?

What do you mean by "your company," which company?

Q. (By Mr. Shearer): Suburban Water.

A. Could you reframe the question, please?

Q. What you did, did you not, Mr. Garnier, was to take preferred stock of your company——

A. Could you state the company names because——

Q. Suburban Water Company, and give the builder who held the right to refunds, preferred stock in trade for the contract of refunds which he held?

A. If my memory is correct, I believe that such

(Testimony of Camille A. Garnier.)

an exchange on a dollar for dollar basis was made with Mr. Brittain, yes, sir.

Mr. Constable: That is all I have.

Mr. Shearer: What is the name?

Mr. Constable: Brittain.

The Witness: I might explain further that this is unique to Suburban Water Systems and is not done by any other company that I know in California. [124]

Q. (By Mr. Shearer): When was this done?

A. Within the last 12 or 16 months.

Q. Prior to that time had there been any like transactions by Suburban Water Company prior to the first exchange of this preferred stock?

A. Yes, sir.

Q. When was the first time that Suburban ever made such an exchange?

A. If I remember correctly, again, the Public Utilities Commission approved the exchange of Suburban Water System securities on a dollar for dollar basis for the outstanding value of a refund agreement in February of 1952. That is the first instance I know of in California.

Q. Now, this Brittain transaction, did it involve a subdivision with which you were familiar?

A. Yes, sir.

Q. Did you appraise the specific factors there involved?

A. Yes, sir. I made many such appraisals.

Q. By the way, what does your preferred stock pay?

(Testimony of Camille A. Garnier.)

A. This is a 3 percent cumulative preferred.

Q. Is it readily marketable?

A. No, it is not.

Q. Is it redeemable at the option of the holder thereof?

A. It is redeemable at the option of the water company. [125] The holder might be the owner.

You mean the owner?

Q. The owner, yes.

A. No, sir. There is no redemption provision, no sinking provisions.

Q. Do you know whether this stock is quoted on any exchange or over the counter?

A. No, sir. What sales are made are made at very considerable discount.

Mr. Shearer: No further questions.

Mr. Constable: That is all, your Honor.

The Court: I have some questions.

Examination

Q. (By the Court): What is your position with the Suburban?

A. I am president and general manager.

Q. How long have you been president and general manager? A. Since 1944.

Q. '44? A. Yes, sir.

Q. Do you have to do with or know of the contracts such as these 1 to 7, Exhibits 1 to 7 show, in this proceeding, the contracts that are of that nature that your company makes?

(Testimony of Camille A. Garnier.)

A. Yes, we have about two million dollars worth outstanding at the present time. [126]

Q. Do you know of any of them that have run for any appreciable percentage of the ten-year period, where there have been no refunds?

A. Yes, sir.

Q. Very many?

A. In answer to that, I have just finished a study of that question for our own office about five months ago, and the results of the study indicated that we have contracts that would pay on the ten-year period, 6½ percent of the face value up to the full payment of the total contract in six years; I mean there is that much variation.

Q. What sort of areas are there where there have been no refunds?

A. There are areas right alongside of each other. It depends on the type of development.

Q. What are the variations?

A. You could have a subdivision — I will give two examples; an example of maximum return and one of minimum. A subdivision wherein there was one street laid with a pipe line going up the center of that street serving houses on both sides, with a cost of approximately $85 per lot, an average rate of $45 to $48 a year.

Q. What do those figures refer to? I don't know what you are meaning by those.

A. Where the cost to the subdivider was $85 per lot [127] for the installation of water mains, and where the consumer paid additionally $45 to $48 for

(Testimony of Camille A. Garnier.)

water service on a 35 percent refund, it meant that that tract paid out in six to seven years.

Now, right alongside of it was a subdivision where, because of the way it was laid out, where it was necessary to lay pipe lines all around the periphery of the tract with lots only on one side of the pipe line, doubling the cost, and where the cost of that tract ran about $180 to $190 a lot, and lots were sold and some houses were built. There were many of those lots at the end of the sixth year, even though the subdivider had sold the lot and received his money therefor, the purchaser had not yet built a residence thereon, and there was no money coming back from it, coming back to the subdivider. And in those instances those tracts paid 20 to 25 percent of the full amount of the deposit. The tract that went——

Q. In other words, where that exists, your experience would be that—your study—they had gotten back in the period 25 percent?

A. Of the full deposit by the end of the tenth year.

Q. All right. Now, contrast that situation with one that is fully built and sales are what might be regarded as normal, namely, the sales of the houses to purchasers.

A. In the case of a subdivider that is going to build the houses at the same time that the mains are installed, the amount of money that would be returned of the total deposit [128] would depend a great deal on the time that that installation was

(Testimony of Camille A. Garnier.)

made, and as an average—again I am speaking as an average over let's say 10,000 services have been installed by our company in the last two or three years, which may not be applicable to this case, which was way prior, and where costs were different and everything else — the refund will be anywhere from 65 percent to about 105, with an average of about 70 to 80, approximately very close with what Mr. Moseley said.

Q. How do you get a refund of 105 percent?

A. Well, because the contract will pay out in full by about eight and a half years.

Q. It doesn't run the full ten-year period?

A. That's correct.

Q. And you are allowing a figure in there to make up for that accelerated repayment?

A. It probably isn't the correct way to state it.

Q. I think that we understand what you mean.

So that in these matters and in making a calculation as to how they are going to pay out, you take into consideration the tract, whether it is built up rapidly and the houses are sold, or whether it is a hit or miss proposition?

A. That is correct.

Q. And those are the extremes probably?

A. That is correct.

Q. And where you have those facts and you know the area, [129] then is it true that you are unable to make some fairly satisfactory calculations as to what will be returned?

(Testimony of Camille A. Garnier.)

A. Yes, your Honor, up until the time that the tract has been fully occupied for about a year and a half to two years, because that eliminates a lot of the factors that should come about, but if everything went right—but that you just can't tell.

Q. Well, does the nature of the area, the demand for homes, the rate at which homes are selling, and factors of that kind, have some enlightening effect on your being able to make such a computation?

A. Yes, sir, they are a big factor in making the computation.

Q. In short, if no house has been built on a subdivision when you complete your mains, but it is in an area that is growing, and houses around on other tracts are selling regularly and there is a demand for them, that would be quite different, wouldn't it, from one that was out somewhere else, and it was an untested area and you couldn't tell what the demand was going to be?

A. Not quite, sir, because within three blocks of our office there are three subdivisions covering about 180 acres that were subdivided seven years ago, and there are still approximately 30 percent of the lots vacant. And yet immediately surrounding them there are other tracts that are selling [130] houses ahead of their construction.

Q. Is there a difference in the contour or the construction or the arrangements and plans of sale as between those areas?

A. Yes, sir, and the type of development that is within the areas.

(Testimony of Camille A. Garnier.)

Q. So those, likewise, are factors that you take into account in computing——

A. Yes, sir, it would be necessary.

There are two things we are talking about. One is the amount of refund and the other is the value of the agreement. The amount of refund is affected by these many factors——

Q. I think that one of your difficulties here—you have been very enlightening—but I think one of your difficulties is that you are trying to answer some of the questions that are involved in this case, rather than questions that relate to this housing and the installation of water and the use of water.

I rather conclude that you have some knowledge of the question that is at issue here on the tax standpoint and that you are letting that creep into your consideration and phrasing of your answers, whereas the Court here is interested in strictly the operation of your water company and these factors that have nothing to do with the tax except by way of result, and how they are dealt with and treated in your making of these contracts and in the making of the refunds to the water users or [131] to the owners of the contracts, whoever it is.

The Court: All right, any questions that counsel may have had suggested by my questioning, you may ask.

Mr. Shearer: No further questions.

Mr. Constable: No questions.

The Court: You are excused.

(Witness excused.)

Mr. Shearer: I will call Mr. Gersten.

ALBERT GERSTEN

was called as a witness by and on behalf of the petitioners, and, having been first duly sworn, was examined and testified as follows:

The Clerk: State your name, please.

The Witness: Albert Gertsen.

Direct Examination

Q. (By Mr. Shearer): Mr. Gersten, state your occupation, please.

A. Subdivider and builder.

Q. How long have you been in the subdivision business? A. About 16 years.

Q. How have you operated with respect to entities?

A. Partnerships, joint ventures, corporations, sole ownerships.

Q. Where has your primary business been conducted? A. Los Angeles County. [132]

Q. You are familiar with what has been called the water facilities contracts, Exhibits 1 to 7?

A. Yes.

Q. You have seen those before? A. Yes.

Q. Apart from the practical need of water which may or may not exist, is there any legal requirement in Los Angeles County to bring water to a subdivision tract?

A. Yes, legal in this way: Unless you bring water in and have it available for each lot, the California Real Estate Commissioner will not issue a permit to sell property.

(Testimony of Albert Gersten.)

Q. Now, Mr. Gersten, have you subdivided properties in areas served by municipally owned water systems? A. Yes.

Q. In those cases do you, a subdivider, pay for the water pipe installations?

A. Yes, in all cases the subdivider must pay in order to have a salable subdivision. That's the first requirement.

Q. In those cases are there any rights to receive refunds contingently or otherwise?

A. No, there are not. In areas specifically which I have a direct knowledge, in the City of Los Angeles, there is no refund of any kind. In the City of Alhambra, where I subdivided, there are no refunds; and so on. There are several others in which there are no refunds, but I was compelled to [133] pay the cost of installations.

Q. Mr. Gersten, directing your attention to the J. Richard Company, what position did you occupy in that company? A. President.

Q. You were familiar with its affairs and its business? A. Yes.

Q. And what position did you occupy in the Lawrence Land Company? A. President.

Q. Were you familiar with its affairs and business? A. Yes.

Q. Both of those corporations were subdividers?

A. Yes, in the subdivision and building business.

Q. In what respect, if any, was the operation of J. Richard Company different from that of Lawrence Land Company?

(Testimony of Albert Gersten.)

A. Different in location of land, different in value of land, both raw and finished, different in the types of houses constructed, different in type of financing obtained, different in the type of sales program, different character of buyers.

The Court: Were they both residential developments?

The Witness: Yes, sir.

Q. (By Mr. Shearer): It has been stipulated that the Lawrence Land Company was incorporated on May 20, 1949 and commenced doing business shortly after that time. On or about May 20, 1949 did the [134] J. Richard Company have any obligations?

A. I don't know at that particular date if J. Richard Company started construction of houses; had a very, very large liability.

Q. Did the J. Richard Company have an obligation with respect to each home it constructed prior to the time it sold that home? A. Yes.

The Court: What do you mean by that?

Mr. Shearer: Had an obligation?

The Court: Yes. I think you better follow that up.

What do you mean by that, Mr. Witness?

The Witness: In our interim financing, we executed notes secured by deeds of trust on each piece of property for an amount given to us, agreed to give us by the lending institution.

In this particular J. Richard Company tract, as I recall now, the obligation or the lien on these

(Testimony of Albert Gersten.)

houses was approximately two million dollars, and those were liabilities of the company and myself until the houses were sold and the new buyer assumed the liability.

The Court: That is a rather normal operation, isn't it?

The Witness: Well, I don't know. There are many, many phases of it. Some builders don't borrow money. They are fortunate to have the expenses to carry themselves.

The Court: But not too many of them. [135]

The Witness: Well, not too many rich people, I suppose.

The Court: I mean, something that is more often than not. I was just a little bit puzzled at the question, but go ahead. Maybe it will clear up for me.

Mr. Shearer: Yes, your Honor.

Q. (By Mr. Shearer): Did the Lawrence Land operation involve Federal Housing Administration commitments?

A. Yes, all of my developments did.

Q. So did the J. Richard Company?

A. Yes, sir.

Q. Did the existence of the obligations outstanding of the J. Richard Company have a bearing upon the obtaining of additional Federal Housing Administration commitments at that time?

The Court: By whom?

Mr. Shearer: I was just about to say by the J. Richard Company.

A. Yes. J. Richard Company could not obtain

(Testimony of Albert Gersten.)

any additional FHA-insured builders' loans because of its rather contingent liability, and for a practical purpose, in our business — and which is general practice, that each subdivision stands on its own. They rarely, in my experience, have any continuing subdivisions, one onto the other, because of the large contingent liability existing during construction period. [136] And in order to obtain FHA firm commitments, in this case on J. Richard Company, the paid-in capital would have had to be so large that very few people I know could meet it, with the result a new subdivision — had a new corporation known as Lawrence Land Company, which at its inception was free to obtain necessary financing and commitments through FHA, based on a certain capitalization.

Q. Now, directing your attention to the water facilities contract again, was there a variation in the time, commencing with the commencement of the water pipe installations and ending with the completion of the houses, completion and sale of the houses in a given tract, as between one subdivision and another? A. Yes.

Q. What factors would create such variations?

A. Well, in our specific cases——

Q. I am directing my attention, I should say, to the period from June 1947 through December 1950.

A. There were shortages, labor shortages, one trade would have to wait upon another; as an example, in the course of subdividing, first is grading; next, sewer installation; next, water. If either of

(Testimony of Albert Gersten.)

the contractors prior to the sewer installers does not have his work done—that is, prior to the water installers—does not have his work done, in that case the water company must wait, of necessity, until these other [137] two things are done.

The time element varies with these conditions, over which no one has control. They may vary four months, six months, three months, I don't know. But there is a different variance.

The Court: Now, you are speaking generally?

The Witness: In our particular subdivision, my personal experience.

Q. (By Mr. Shearer): Is that statement also applicable in general to subdivisions in Los Angeles County, if you know? A. Yes, I think so.

Q. Would such things as strikes be a factor?

A. Yes.

Q. Would material shortages be a factor?

A. Yes.

The Court: Those things, of course, follow as a matter of course, that they would be a factor in completion of construction. I think you could almost say as a matter of reason and logic that that would be true.

Mr. Shearer: Yes, your Honor, I think so too, but I can't be so sure that your Honor thinks so until your Honor says so.

The Court: Well, but I don't know whether that still has to do with this case or not, other than just a generalized statement. Of course, if they happened, why—— [138]

(Testimony of Albert Gersten.)

Mr. Shearer: I think the point is, not whether they happen, but the fact if they happen from time to time, and their inability to predict. That is what I am concerned about here, is the difficulties of prediction. I tried to bring that out.

The Court: We are concerned here with the difficulties of prediction with respect to these particular tracts. We don't have any other tracts involved here; we have these tracts. That is where these water contracts are related to. There are seven of them here.

Mr. Shearer: I think there are six — seven exhibits.

The Court: Six tracts, that is right.

Mr. Shearer: Yes.

The Court: You can have all sorts of generalized statements. If it didn't happen to these, then, that would present a different situation.

Mr. Shearer: Well, I will reserve that——

The Court: That is one of the troubles. We are getting a lot of generalized discussion here, where, as a matter of fact, we are dealing with specific property and the contracts relating to them.

Mr. Shearer: I think that is a matter that I will have to take up on brief.

The Court: I rather assume so.

Mr. Shearer: I don't entirely agree with your Honor, but [139] I have had the advantage of carefully going over the stipulation, and for that reason——

The Court: Of course, I don't know — if those

(Testimony of Albert Gersten.)

things are covered in the stipulation with respect to these particular tracts, why, then, that would take care of that.

Q. (By Mr. Shearer): Mr. Gersten, during the period from June 10, 1947 through December 1950, were there any strikes affecting the building industry? A. Yes, definitely.

Q. Now, were those strikes predicted prior to the time they happened? A. No.

Q. Now, did the outbreak of the Korean situation in 1950 have a bearing upon availability of materials? A. Very definitely.

Q. In what respect?

A. Shortages resulted in slowups, that certain crafts—steel, for instance, couldn't be delivered to a job; cement was in short supply, with the result that trades had to wait a longer period of time to make its installations, and specifically has affected these tracts in this matter, in this case. We had a painters' strike that resulted in a delay in Lawrence Land Company, a delay in completing that tract about four months. We had a strike in J. Richard Company—a general [140] strike was called on one of our tracts—I think it was 15062—that delayed the construction. And in that case we required a lengthy court proceeding against the union.

Q. Referring to the strike affecting the J. Richard Company, did that strike break out after the water pipe line contract had been started?

A. Yes.

(Testimony of Albert Gersten.)

Q. In referring to the strike affecting Lawrence Land Company, did that strike break out after the water pipe installations had commenced?

A. Yes, quite a time after that.

Mr. Shearer: No further questions.

Cross Examination

Q. (By Mr. Constable): I think you mentioned that the Korean war broke out in 1950. That was June, around June 25, 1950, wasn't it?

A. I should remember, but I presume that was it.

Q. Yes, and you also testified that there was a slowup in your building, caused by a shortage of materials and all of the other factors which result from a wartime economy, is that correct?

A. That there were shortages?

Q. Yes, and a consequent slowup in building, in general? A. Yes.

Q. Home building? [141] A. Yes.

Q. Now, as a result of that, it is also true, isn't it, Mr. Gersten, immediately that the Korean war broke out and that building shortages were anticipated, owning homes became in demand?

A. Homes became in demand, but the ability to construct them and deliver them was still the same. I mean our sales at times were ahead of our production, but because of these slowups we could not deliver the house, and it resulted in many cancellations.

(Testimony of Albert Gersten.)

Q. I see. And these slowups occurred, then, after the outbreak of the Korean war?

A. They occurred generally from 1947 through 1950, '51.

Q. The Korean war slowups?

A. No, the shortages. Shortages were created by the—at the closing of the war, and when building got an O.K. there were shortages constantly, and delays.

Mr. Constable: That is all I have, sir.

The Court: You are excused.

(Witness excused.)

Mr. Shearer: Subject to the proposed stipulation that I offered respecting the item that came up regarding Mr. Moseley's testimony, petitioner rests.

Mr. Constable: I have no witnesses, your Honor, but I didn't quite understand the last statement Mr. Shearer made. [142]

Mr. Shearer: I offered a stipulation to which counsel agreed to consult, and subject to being able to stipulate or asking permission to cover it by evidence if we are unable to stipulate——

The Court: I see no reason why it can't be stipulated, and of course if the parties draw up a stipulation covering the facts they can file it.

Mr. Shearer: I see no reason why it can't be stipulated either. I don't know what the facts are, but I assume the water company does.

The Court: Well, they ought to. They have a record of their contracts down there. It would be a strangely operated company if they didn't.

Mr. Shearer: I don't think there is any question that they do.

Mr. Constable: I think respondent has stated its position in that connection.

The Court: All right.

Mr. Constable: I am going to withdraw some exhibits.

The Court: Do you have anything to offer?

Mr. Constable: No.

The Court: You say you have no witnesses. Do you have any other evidence?

Mr. Constable: Nothing.

The Court: All right. You both rest, then, I take it, [143] subject to the fact that you are going to get together on a stipulation with respect to those items from the water company books?

Mr. Shearer: Yes, your Honor.

The Court: Now, this is going to be a bad case to work. There are main issues running with one group, main issues running with another group of these proceedings, and then there are side issues that relate to individual proceedings, and I don't know how much of your stipulation is a stipulation of evidence and how much is a stipulation of facts. We have gotten into the habit of referring to stipulations as being stipulations of fact, even though very often they are stipulations of evidence, and not true stipulations of fact.

Since it is an involved matter, I want you gentlemen to do me a very good job, a very careful job on proposed findings, because even in the most difficult cases, insofar as the law is concerned, and much

more often than not, your case is decided when the facts are found and you don't have—when the facts are found definitely and clearly, you don't have nearly so much trouble with the application of the law. Sometimes you don't have any. So I want you to take whatever time is needed for doing a good job.

I am going to be just as much interested in the job on your proposed findings as I am in this very deep discourse on the law that I anticipate coming with the questions here involved. [144] And I would like for you to take that stipulation of facts, and to the extent that it is a stipulation of evidence, namely, an agreement of evidence that is to go in or evidence that has come in by agreement, and from that evidence find the facts just the same as you think they ought to be found, propose the facts that you think ought to be found from that, just the same as you propose the facts that you think should be found from the oral testimony, so that I will have a completed job, and not have to wade through documentary stuff and sort out and make findings myself.

Now, how much time do you think you will need to do your job?

Mr. Constable: May I ask what kind of briefs the Court will order?

The Court: Well, I normally prefer the first brief by the party who is the moving party, and usually that is the petitioner in the proceedings before us, but I have found that I don't get as good briefs from the respondent that way as I do having

simultaneous briefs and then replies. So I have, over the last year or two, gradually been abandoning my former practice of having the moving party file a brief and then the other party respond or reply.

If I could be assured of getting good answering briefs that way, I might continue it, but unless I have some reason, otherwise I am going to have to ask for simultaneous briefs with [145] reply.

Mr. Constable: Mr. Shearer and I have talked about this during the stipulation of fact, and we arrived at a few points, at which time I informed him, because of that, I would like seriatim briefs.

The Court: The difficulty with that is, I never get a reply out of the respondent.

Mr. Constable: I might say, your Honor, I would like seriatim briefs on the arguments of the joint return, on the excess profits tax, and a simultaneous brief on the facts, so I think simultaneous briefs would be satisfactory to the respondent.

The Court: Well, I am going to set it that way. How much time do you think you will need?

I may say that I am very heavily loaded with submitted cases, and you might just as well ask for as much time as you need now and not have to file a motion for extension of time.

Mr. Constable: I had a case this morning in which I was given 90 days. This case, then, I suppose——

The Court: That case this morning was a simple case compared to this one.

Mr. Constable: That is correct, your Honor.

I think it could be set about the same time, as far as I am concerned.

Mr. Shearer: I am inclined to think a little longer time than that. [146]

The Court: 120 days?

Mr. Shearer: 120 days, partly because I have cases coming up on the next two calendars that will take up a considerable part of my time.

The Court: Very well, 120 days, with 45 for reply. And I want good reply briefs from both of you.

The case stands submitted upon the filing of briefs.

Mr. Constable: Your Honor, would the Clerk prefer that I withdraw these exhibits off the record or in the record?

The Clerk: Either way.

Mr. Constable: I can tell you what they are.

The Court: Well, you make your arrangements with the Clerk. The withdrawal of returns and exhibits that are readily susceptible of having photostats substituted is a matter of usual practice here, and unless there is some reason or otherwise, you make your arrangements so that the record is preserved, the integrity of the record is maintained, and that is all that is necessary. There should be no difficulty.

So you make your arrangements with the Clerk, and unless there is something further, then, that concludes the business until we call the Palmer case at 10:00 o'clock on Monday morning, as I understand it.

The Clerk: That is correct.

Mr. Shearer: There may be some difficulty, your Honor, in obtaining the information requested of the water company, and I [147] assume we can simply mail that stipulation on.

The Court: What is done rather regularly in Division 8—and I happen to be Division 8—is that where there is a matter that indicates by its very character that it is readily susceptible of stipulation, the parties regularly work it up. If they can get it done before I leave, that is very good. If they don't, they merely attach a motion and send it in, say "Herewith is a stipulated matter," and that thereby becomes a part of the record, because I grant it. I have never had any difficulty. It always works nicely, and I don't think you should have any difficulty on that here.

If you get it finished before I leave, fine; if you don't, fix it up and send it in.

If there is nothing further, then,——

The Clerk: The respondent has withdrawn all of his exhibits from A through Y, and Petitioners' Exhibit No. 8. The respondent has these exhibits and will forward them to Washington.

The Court: We will stand adjourned.

(Whereupon, at 5:55 o'clock p.m., the hearing in the above-entitled petition was closed.)

[Endorsed]: T.C.U.S. Filed May 17, 1955.

[Title of Tax Court and Docket No. 51226.]

DESIGNATION OF CONTENTS OF RECORD ON REVIEW

To The Clerk of The Tax Court of the United States:

You will please prepare, transmit, and deliver to the Clerk of the United States Court of Appeals for the Ninth Circuit copies duly certified as correct of the following documents and records in the above-entitled cause in connection with the petition for review heretofore filed by the Taxpayer:

(1) The docket entries of all proceedings before the Tax Court.

(2) Pleadings before the Tax Court, as follows:

(a) Petition.

(b) Answer.

(3) The findings of fact and opinion of the Tax Court.

(4) The decision of the Tax Court.

(5) The petition for review.

(6) Written stipulation of facts entered into by petitioner and respondent, exclusive of the following paragraphs: 9, 10, 11, 12, 21, 22, 23, 24, 31, 32, 33, 34, 35, 42, 43, 44, 45, 48, 49, 50, 51, 52, and 74.

(7) Supplemental Stipulation of Facts.

(8) All Exhibits other than Respondent's Exhibits A through P, both exclusive.

(9) The entire official transcript of oral testimony including statements and stipulations of counsel and of the trial Judge.

(10) This designation of contents of record on review.

/s/ JACOB SHEARER,
Attorney for Petitioner.

Of Counsel:
TANNENBAUM, STEINBERG & SHEARER.

Affidavit of Service by Mail Attached.

[Endorsed]: T.C.U.S. Filed Feb. 5, 1958.

[Note: Designation of Contents of Record on Review in Docket Nos. 51228 and 51229, filed Feb. 6, 1958, are the same as Docket No. 51226, set out at pages 256-7.]

[Title of Tax Court and Docket Nos. 51226, 51228, 51229.]

CERTIFICATE

I, Howard P. Locke, Clerk of the Tax Court of the United States, do hereby certify that the foregoing documents, 1 to 24, inclusive, constitute and are all of the original papers on file in my office as called for by the "Designation of Contents of Record on Review" and "Designation of Additional Portions of Record on Review" excepting exhibits, which are separately certified, on file in my office as the original and complete record in the cases before the Tax Court of the United States docketed at the above numbers and in which the petitioners in the Tax Court have filed petitions for review, as above numbered and entitled, together with a true

copy of the docket entries in said Tax Court cases as the same appear in the official docket in my office.

In testimony whereof, I hereunto set my hand and affix the seal of the Tax Court of the United States, at Washington, in the District of Columbia, this 26th day of February, 1958.

[Seal] /s/ HOWARD P. LOCKE,
Clerk, Tax Court of the
United States.

[Endorsed]: No. 15945. United States Court of Appeals for the Ninth Circuit. Albert Gersten, Myron P. Beck and Ann H. Beck, Milton Gersten and Mary Gersten, Petitioners, vs. Commissioner of Internal Revenue, Respondent. Transcript of Record. Petitions to Review Decisions of The Tax Court of the United States.

Filed: March 17, 1958.

Docketed: March 21, 1958.

/s/ PAUL P. O'BRIEN,
Clerk of the United States Court of Appeals for the Ninth Circuit.

In The United States Court of Appeals
For The Ninth Circuit

No. 15945

ALBERT GERSTEN, MYRON P. BECK, and ANN H. BECK, MILTON GERSTEN and MARY GERSTEN, Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent.

STATEMENT OF POINTS

Albert Gersten, Myron P. Beck and Ann H. Beck, and Milton Gersten and Mary Gersten, the Petitioners herein, by their attorney, Jacob Shearer, hereby assert the following errors, which they intend to urge on review by the United States Court of Appeals for the Ninth Circuit of the decision of the Tax Court of the United States in the above causes, Tax Court Docket Numbers, 51226, 51228 and 51229, on October 30, 1957.

1. Rights under certain contracts were assigned and distributed to petitioners upon the dissolution and liquidation of certain corporations of which they were stockholders. Said rights consisted of the right to receive monies upon the happening of and measured by certain contingent future events provided for in the contracts, similar to the rights under the contracts in issue in the case of Westover v. Smith, 173 F. 2d 90 (C.C.A. 9, 1949). The Tax Court erred in determining that such rights had ascertainable fair market values for the

purpose of determining petitioners' capital gains on the dates of the distributions in final liquidation, respectively, by said corporations.

2. During the year 1950, petitioner Albert Gersten married Bernice Ann Gersten in Mexico, immediately following a divorce decree, which he obtained in Mexico, dissolving his marriage to Lucille Gersten. Under California law, Albert Gersten was estopped from obtaining and could not have obtained an annulment of the marriage to Bernice Ann Gersten and was estopped from asserting, for property and status purposes, that he was not married to Bernice Ann Gersten. The Tax Court erred in determining that Respondent was a proper person entitled to challenge the validity or existence of the marriage and further in determining that petitioner Albert Gersten and Bernice Ann Gersten were not entitled to file a joint return as husband and wife, pursuant to Section 51(b) of the Internal Revenue Code of 1939.

Dated at Beverly Hills, California, this 20th day of March, 1958.

/s/ JACOB SHEARER,
Attorney for Petitioners.

Of Counsel:
TANNEBAUM, STEINBERG &
SHEARER.

Affidavit of Service by Mail Attached.

[Endorsed]: Filed March 21, 1958. Paul P. O'Brien, Clerk.

[Title of Court of Appeals and Cause.]

DESIGNATION OF CONTENTS OF RECORD

Albert Gersten, Myron P. Beck and Ann H. Beck, Milton Gersten and Mary Gersten, the respective petitioners herein, by their attorney, Jacob Shearer, hereby adopt, as their designation of the record in the above entitled causes, the "Designation of Contents of Record on Review" respectively filed by them with the Clerk of the Tax Court of the United States in Tax Court Docket Nos. 51226, 51228 and 51229 respectively, and copies of which were duly served upon counsel for Respondent. Said Designations have been certified and transmitted by the Clerk of said Tax Court to the Clerk of the above entitled Court.

Dated at Beverly Hills, California, this 20th day of March, 1958.

/s/ JACOB SHEARER,
Attorney for Petitioners.

Of Counsel:
TANNENBAUM, STEINBERG & SHEARER.

Affidavit of Service by Mail Attached.

[Endorsed]: Filed March 21, 1958. Paul P. O'Brien, Clerk.